IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1361

CALVERT FIRE INSURANCE COMPANY,
A PENNSYLVANIA CORPORATION,
Petitioner,

v.

AMERICAN MUTUAL REINSURANCE COMPANY,
AN ILLINOIS CORPORATION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE ILLINOIS APPELLATE COURT

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PETITION FOR A WRIT OF CERTIORARI TO THE ILLINOIS APPELLATE COURT

The Petitioner, Calvert Fire Insurance Company, an Illinois corporation ("Calvert"), by its counsel, prays that a writ of certiorari issue to review a judgment of the Illinois Appellate Court, First District, Fourth Division, that affirmed orders of the Circuit Court of Cook County striking and dismissing portions of the Petitioner's answer and counterclaim.

OPINION BELOW

The opinion of the Illinois Appellate Court and its supplemental opinion denying a petition for rehearing (both in App. G) are reported in 52 Ill. App. 3d 922, 367 N. E. 2d 104.

The oral opinion of the Illinois Circuit Court (App. A) is unreported.

JURISDICTION

On October 12, 1977, the Illinois Appellate Court denied a certificate of importance (App. H) under Illinois Supreme Court Rule 316, Ill. Rev. Stat. 1975, c. 110A, §316, which would have allowed appeal of the Appellate Court's interlocutory order; and on January 26, 1978, the Illinois Supreme Court denied a petition for leave to appeal (App. I) under its Rule 315, *id.*, §315. This Court's jurisdiction is invoked under §2101(c) of the Judicial Code, 28 U. S. C. §2101(c).

QUESTIONS PRESENTED

(1) Is an interest in a reinsurance pool of 100 insurance companies, which look for a profit solely to the efforts of the reinsurer that promoted and manages the pool, a "security" within the meaning of §2(1) of the Securities Act of 1933 ("the 1933 Act"), 15 U. S. C. §77(b)(1), and §3(a)(10) of the Securities Exchange Act of 1934 ("the 1934 Act"), 15 U. S. C. §78c(a)(10)?

(2) For purposes of the registration requirement of §5 of the 1933 Act, 15 U. S. C. §77e, is such an interest an "insurance * * * policy" exempted by §3(a)(8) of that Act, 15 U. S. C. §77c(a)(8)?

(3) To the extent that the registration and antifraud provisions of the 1933 and 1934 Acts apply, is their application barred by the McCarran-Ferguson Act, 15 U. S. C. §1012(b)?

STATUTORY PROVISIONS INVOLVED

Securities Act of 1933, §2(1), 15 U. S. C. §77b(1):

> SEC. 2. When used in this title, unless the context otherwise requires—

> (1) the term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

Securities Act of 1933, §3(a)(8), 15 U. S. C. §77c(a)(8):

> SEC. 3. (a) Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:
>
> * * *
>
> (8) Any insurance or endowment policy or annuity contract or optional annuity contract, issued by a corporation subject to the supervision of the insurance commissioner, bank commissioner, or any agency or officer performing like functions, of any State or Territory of the United States or the District of Columbia; * * *.

Securities Act of 1933, §5, 15 U. S. C. §77e:

> SEC. 5. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—
>
> (1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or
>
> (2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.
>
> (b) It shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to carry or transmit any prospectus relating to any security with respect to which a registration statement has been filed under this title, unless such prospectus meets the requirements of section 10; or

(2) to carry or cause to be carried through the mails or in interstate commerce any such security for the purpose of sale or for delivery after sale, unless accompanied or preceded by a prospectus that meets the requirements of subsection (a) of section 10.

(c) It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 8.

Securities Exchange Act of 1934, §3(a)(10), 15 U. S. C. §78c(a)(10):

SECTION 3. (a) When used in this title, unless the context otherwise requires—

* * *

(10) The term "security" means any note, stock, treasury stock, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit, for a security, or in general, any instrument commonly known as a "security"; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange,

or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited.

Securities Exchange Act of 1934, §10(b), 15 U. S. C. §78j(b):

SECTION 10. It shall be unlawful for any person directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

* * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule 10b-5, 17 C. F. R. §240.10b-5, adopted under Securities Exchange Act of 1934, §10(b):

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

McCarran-Ferguson Act, §2(b), 15 U. S. C. §1012(b):

(b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the

purpose of regulating the business of insurance, or which imposes a fee or tax upon such business, unless such Act specifically relates to the business of insurance: *Provided*, That after June 30, 1948, the Act of July 2, 1890, as amended, known as the Sherman Act, and the Act of October 15, 1914, as amended, known as the Clayton Act, and the Act of September 26, 1914, known as the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

STATEMENT OF THE CASE

The Facts

Unless other references are cited, the facts are taken from the opinion of the Illinois Appellate Court, which noted that, "in determining the sufficiency of the answer and counterclaim when attacked by a motion to strike or dismiss, all well pleaded facts are taken as true." 52 Ill. App. 3d at 924, 367 N. E. 2d at 107, p. G-3 *infra*.

Calvert is a Pennsylvania corporation engaged in writing property and casualty insurance. The Respondent, American Mutual Reinsurance Company ("American Mutual"), is an Illinois corporation engaged solely in the business of reinsuring property and casualty risks insured by other companies. For some years prior to 1974 American Mutual, in order to increase the volume of its business beyond its own capacity, annually promoted a so-called "Multiple Line Pool." Participants in the pool were entitled to a specified percentage of the pool's profits in exchange for their promise to indemnify American Mutual against a specified percentage of losses. As sole promoter and manager of the pool, American Mutual received 4½% of premiums earned.

In January of 1974, as a result of solicitations by American Mutual representatives carried on in person as well as by telephone and mail, Calvert joined 99 other insurance companies

in a "Multiple Line Reinsurance Participating Agreement" with American Mutual. A few months later, on discovering from American Mutual's 1973 annual report that it had made major changes in its methods of accounting and creating reserves for incurred losses not reported, Calvert repudiated the contract.

American Mutual thereupon sued Calvert in the Circuit Court of Cook County, Illinois, for a declaratory judgment sustaining the validity of the contract (App. A). Calvert's answer and counterclaim (App. B) pleaded both fraudulent inducement and—on the theory that interests in the pool were "securities"—violation of the registration requirements of §5 of the 1933 Act and the Illinois and Maryland blue sky laws. On the same theory, the fraud allegations were based on Rule 10b-5, 17 C. F. R. §240.10b-5, adopted under §10(b) of the 1934 Act, 15 U. S. C. §78j(b), as well as common law deceit.

On the same day Calvert filed its own action against American Mutual in the United States District Court for the Northern District of Illinois in which it pleaded the same grounds, except that it had been careful in the state court, on account of the exclusive jurisdiction given the federal courts by §27 of the 1934 Act, 15 U. S. C. §78aa, to plead Rule 10b-5 only by way of defense and not in its counterclaim.

Judge Will in the District Court stayed the federal proceedings pending the outcome of the state proceeding. One result of his action was the issuance of a writ of mandamus by the Court of Appeals for the Seventh Circuit, *Calvert Fire Ins. Co.* v. *Will*, 560 F. 2d 792 (1977), which is now awaiting argument in this Court pursuant to a writ of certiorari (No. 77-693). Another result of Judge Will's action was that Calvert had no choice but to defend itself in the ongoing state proceeding.

On the state side, the Circuit Court of Cook County dismissed Calvert's counterclaim and struck the defenses going to the federal and state securities laws on the grounds (1) that no "security" was involved and (2) that application of the federal securities laws was barred by the McCarran-Ferguson Act, 15

U. S. C. §1012(b) (Apps. C-E). But it considered those questions sufficiently substantial to warrant an interlocutory appeal under Illinois Supreme Court Rule 308, Ill. Rev. Stat. 1975, c. 110A, §308 (App. F). The Illinois Appellate Court affirmed and denied a petition for rehearing (App. G). *American Mutual Reinsurance Co.* v. *Calvert Fire Ins. Co.*, 52 Ill. App. 3d 922, 367 N. E. 2d 104 (1977). And both that court (App. H) and the Supreme Court of Illinois (App. I) declined to permit review by the latter court.

REASONS FOR GRANTING THE WRIT OF CERTIORARI

I. The Court May Wish to Consider This Case with Will v. Calvert Fire Ins. Co. (No. 77-693).

First: We are sensitive to the fact that it would be unusual for this Court to use its certiorari jurisdiction in order to review an interlocutory decision of an intermediate state court. The special circumstance that has impelled the filing of this petition is the relationship of this case to *Will* v. *Calvert Fire Ins. Co.*, in which a petition for a writ of certiorari has already been granted (No. 77-693). Since all that Calvert is seeking in that case is a federal court's determination of the "security" question—over which the federal courts' jurisdiction is exclusive so far as the 1934 Act is concerned—the essential purpose of this petition is to put the Court in a position, if it is so disposed, to cut through to the merits by way of review of the state court's determination of the "security" question.

Second: So far as the interlocutory character of the judgment in question is concerned, the strict liability that §12(1) of the 1933 Act, 15 U. S. C. §77*l*(1), provides for violation of §5 makes the judgment substantially final; for it is undisputed that nothing was ever registered under the 1933 Act. If this Court should determine that an interest in the pool was a "security" within the meaning of the 1933 Act, §12(1) would dictate automatic rescission of the contract. And, if this Court were to

reach the opposite conclusion, Calvert would be relegated to establishing common law fraud.

Third: So far as the intermediate status of the Illinois Appellate Court is concerned, Calvert did petition the Illinois Supreme Court for leave to appeal, without success, and there is no assurance that that court would grant such a petition even after trial and a decision by the Appellate Court on the merits; for the "leave to appeal" procedure under that court's Rule 315, Ill. Rev. Stat. 1975, c. 110A, §315, is comparable to this Court's certiorari procedure. Moreover, even if the Illinois Supreme Court were to grant leave to appeal after the Appellate Court's review of a final judgment, we venture to suggest that this Court has had considerably more experience with both the "security" question and the McCarran-Ferguson Act.

II. The State Court Has Construed the Federal Definition of "Security" in a Way Not in Accord with Decisions of This Court.

First: The definition of "security" is, of course, central to the whole scheme of federal securities regulation.[1] Witness the fact that this Court has construed the term in no fewer than six cases and has recently granted certiorari in a seventh case.

In the first five of these cases—in all of which the Court (reversing the Courts of Appeals) emphasized the importance of a broad reading of the definition in order to prevent evasion of the statutory purpose—the Court found the presence of an "investment contract" and hence a "security" in schemes involving sales of real property interests by metes and bounds,[2] variable

1. The question thus presented has broad ramifications; for the total reinsurance premiums written in the United States in 1975 was in excess of $4.5 billion, and the volume of reinsurance written increased by 334% between 1960 and 1975.

2. *SEC* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344 (1943) (oil leaseholds); *SEC* v. *W. J. Howey Co.*, 328 U. S. 293 (1946) (orange grove tracts).

and so-called "flexible fund" life insurance policies,[3] and capital shares issued to evidence savings accounts in a savings and loan association.[4] And the case now pending involves a holding by the Court of Appeals for the Seventh Circuit that interests in employee pension plans are "securities."[5]

Second: The decision below is at odds with the test that was laid down in the *Howey* case (*supra* note 2), the second in the series, and that has been universally followed (and sometimes extended) by the lower federal courts, as well as the state courts in construing the "investment contract" term as used in the state blue sky laws' similar definitions of "security": whether the "contract, transaction or scheme [is one] whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed by the enterprise." 328 U. S. at 298-99.[6]

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3. *SEC* v. *Variable Annuity Life Ins. Co. of America*, 359 U. S. 65 (1959); *SEC* v. *United Benefit Life Ins. Co.*, 387 U. S. 202 (1967).

4. *Tcherepnin* v. *Knight*, 389 U. S. 332 (1967).

5. *International Brotherhood of Teamsters* v. *Daniel*, No. 77-753.

6 The use of the term "money" was fortuitous. In most cases, it may be assumed, the investor (as in *Howey*) in fact parts with money. But that is not always true:

(a) Securities are frequently issued in exchange for other securities. Witness the exemptions for various kinds of exchanges in §§3(a)(9) and 3(a)(10) of the 1933 Act, 15 U. S. C. §77c(a)(9)-(10).

(b) In *Errion* v. *Connell*, 236 F. 2d 447 (9th Cir. 1956), Rule 10b-5 was applied to an exchange of stock for land.

(c) In *El Khadem* v. *Equity Securities Corp.*, 494 F. 2d 1224 (9th Cir. 1974), Rule 10b-5 was applied to a scheme whereby the plaintiff used the proceeds of a loan from Nationwide Investment Corporation to buy mutual fund shares that were pledged as collateral for the loan, with power in Nationwide to rehypothecate the collateral for its own business purposes. Just as the plaintiff there "supplied Nationwide with cash

This test was reaffirmed in the most recent decision of this Court, *United Housing Foundation, Inc.* v. *Forman*, 421 U. S. 837 (1975), which involved "stock" in a nonprofit housing cooperative purchased solely to acquire subsidized low-cost living space. Repeatedly citing *Howey*, the Court stated (421 U. S. at 858):

> There is no doubt that purchasers in this housing cooperative sought to obtain a decent home at an attractive price. But that type of economic interest characterizes every form of commercial dealing. What distinguishes a security transaction—and what is absent here—is an investment where one parts with his money in the hope of receiving profits from the efforts of others, and not where he purchases a commodity for personal consumption or living quarters for personal use.

Third: The existence of a "security" is not precluded by the fact that reinsurance is an aspect of the insurance industry:

(1) The simplistic "either/or" approach of the state court ignored this Court's analysis of the insurance-security dichotomy. As Mr. Justice Brennan stated in his concurring opinion in the *Variable Annuity* case (*supra* note 3), "It is rather meaningless to view the problem as one of pigeonholing these contracts in one category or the other. Obviously they have elements of conventional insurance * * *." 359 U. S. at 80. And this truism was reflected by a unanimous Court in the *United Benefit* case (*supra* note 3) when it said that "Two entirely distinct promises are included in the contract * * *." 387 U. S. at 207.

(2) Insofar as the pool agreement involved insurance, it must not be overlooked that Calvert was an insurer, not an

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and securities, in the form of prepaid interest and rehypothecatable collateral, and the use of her credit, in the form of an assignable promissory note, to capitalize Nationwide's business ventures" (494 F. 2d at 1226), all in return for Nationwide's management services, so here the undertakings by Calvert and the other pool participants to indemnify American Mutual against pool losses provided American Mutual with capital to expand its reinsurance business.

insured. That is to say, American Mutual was *buying* insurance but *selling* securities. What it was selling was comparable to an interest in a limited partnership, with American Mutual, as sole manager of the enterprise, playing the role of general partner and the participants in the pool playing the passive role of limited partners.

The use of the limited partnership device as a form of tax shelter, with the attendant registration of limited partnership interests under the 1933 Act, has become commonplace. See R. Haft, *Tax Sheltered Investments: Taxation-Securities* (1973); Long, *Partnership, Limited Partnership, and Joint Venture Interests As Securities,* 37 Mo. L. Rev. 581 (1972). If the phrase, "certificate of interest or participation in a profit-sharing agreement," which is a sister phrase to "investment contract," means anything, it surely includes the interests of limited partners, who *ex hypothesi* must rely on the general partner to manage the enterprise if they are not to be liable without limit as general partners themselves. Rule 3a11-1 under the 1934 Act, 17 C. F. R. §240.3a11-1, specifically includes a "limited partnership interest" in the definition of "equity security." Indeed, in *United States* v. *Wernes,* 157 F. 2d 797, 799 (7th Cir. 1946), an offering of limited partnership interests resulted in the affirmance of a conviction under the fraud section of the 1933 Act.

(3) The fact that capital shares issued to evidence savings and loan association accounts are an integral part of the savings and loan industry did not prevent the court in *Tcherepnin* v. *Knight,* 389 U. S. 332 (1967), from holding that those shares were "securities."

(4) The fact that all the investors in the pool were insurance companies might be relevant, under the "needs" test of *SEC* v. *Ralston Purina Co.,* 346 U. S. 119 (1953), in determining whether an exemption from 1933 Act registration was available under §4(2) of that Act, 15 U. S. C. §77d(2), because of the absence of a "public offering." Thus, in the case of offerings to institutional investors—many of which are insurance companies

—the approach of the SEC has been a liberal one. See 1 Loss, *Securities Regulation* 663 (2d ed. 1961). But American Mutual has not claimed the exemption. And, far from there being any comparable exemption from the *fraud* provisions of either the 1933 Act or the 1934 Act, the Second Circuit emphasized in a leading case under Rule 10b-5 that even "speculators and chartists * * * are * * * 'reasonable' investors entitled to the same legal protection afforded conservative traders." *SEC* v. *Texas Gulf Sulphur Co.,* 401 F. 2d 833, 849 (2d Cir. 1968), *cert. denied,* 394 U. S. 976 (1969).

(5) With respect to the exemption in §3(a)(8) of the 1933 Act for "Any insurance * * * policy or annuity contract * * *, issued by a corporation subject to the supervision of the insurance commissioner * * * of any State * * *":

(a) If the pool interests here were "insurance policies," they would not need §3(a)(8). For that exemption, as this Court stated *obiter* in *Tcherepnin* v. *Knight,* 389 U. S. at 342, n. 30 (1967), is "clearly supererogation."

(b) Conversely, if the pool interests meet the "security" test, the *Variable Annuity* and *United Benefit Life* cases (*supra* note 3) are equally clear that they are not the kind of "insurance policy" contemplated by §3(a)(8).

(c) In any event, §3(a)(8), which purports to exempt only from registration under the 1933 Act, cannot affect Rule 10b-5 under the 1934 Act.

III. The State Court Has Construed the McCarran-Ferguson Act in a Way Not in Accord with Decision of This Court.

First: It is of critical importance to two major facets of the economy—the insurance industry and the world of securities—that Congress' deference to state regulation of the "business of insurance" in the McCarran-Ferguson Act not be allowed to get out of hand as a result of state courts' overly broad construction that misreads or (worse) ignores the decisions of this Court.

Second: The state court, perhaps because it considered the McCarran-Ferguson question before it came to the "security" point, overlooked the logic of the *Variable Annuity* case—joined here by *SEC* v. *National Securities, Inc.*, 393 U. S. 453 (1969) —to the effect that insofar as insurance companies sell "securities" (or solicit proxies from their stockholders) they are not engaged in the "business of insurance."

How could it be otherwise? It has never been suggested that the McCarran-Ferguson Act excuses registration under the 1933 Act when insurance companies issue stock or other conventional securities to raise capital for their business operations. Capital procurement is not peculiar to insurance companies. And the pool participations here certainly were a device for raising capital (in the form of the pool participants' obligation to indemnify American Mutual against losses) so as to increase the amount of reinsurance business that it could do.

Third: Even if American Mutual's fund-raising *was* the "business of insurance," the state court did not address—it simply ignored—the teaching of *National Securities* that the McCarran-Ferguson Act still would not bar application of the securities statutes' fraud provisions (or *a fortiori*, by analogy to the proxy rules involved in *National Securities*, the registration provisions):

> It is clear that any "impairment" in this case is a most indirect one. The Federal Government is attempting to protect security holders from fraudulent misrepresentations; Arizona, insofar as its activities are protected by the McCarran-Ferguson Act from the normal operations of the Supremacy Clause, is attempting to protect the interests of the policyholders. Arizona has not commanded something which the Federal Government seeks to prohibit. It has permitted respondents to consummate the merger; it did not order them to do so. In this context, all the Securities and Exchange Commission is asking is that insurance companies speak the truth when talking to their shareholders. The paramount federal interest in protecting shareholders is in this situation perfectly compatible with the

> paramount state interest in protecting policyholders. [393 U. S. at 463.]

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX A

STATE OF ILLINOIS }
COUNTY OF COOK } ss:

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
County Department, Law Division

AMERICAN MUTUAL REINSURANCE COMPANY, Individually, and for the use of 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool, *Plaintiff,* *vs.* CALVERT FIRE INSURANCE COMPANY, *Defendant.*	No. 74 L 10737 Extraordinary Remedy

COMPLAINT FOR DECLARATORY JUDGMENT

Now comes the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, sometimes referred to herein as AMRECO, Individually, and for the use of ALL AMERICAN INSURANCE COMPANY, ALLENDALE MUTUAL INSURANCE COMPANY, ALL-STAR INSURANCE COMPANY, AMBASSADOR INSURANCE COMPANY, AMERICAN CONTINENTAL INSURANCE COMPANY, AMERICAN HARDWARE MUTUAL INSURANCE COMPANY, AMERICAN HOME ASSURANCE COMPANY, AMERICAN MUTUAL FIRE INSURANCE COMPANY, AMERICAN MUTUAL LIABILITY INSURANCE COMPANY, THE AMERICAN STAR INSURANCE COMPANY, ARGONAUT INSURANCE COMPANY, ASSOCIATED MU-

TUAL INSURANCE COMPANY, AUDUBON INSURANCE COMPANY, AUSTIN MUTUAL INSURANCE COMPANY, BENEFICIAL FINANCIAL INSURANCE COMPANY, CAMERON MUTUAL INSURANCE COMPANY, THE CAPITAL FIRE INSURANCE COMPANY, CASUALTY RECIPROCAL EXCHANGE, CENTRAL MUTUAL INSURANCE COMPANY, CITIZENS MUTUAL INSURANCE COMPANY, CITIZENS SECURITY MUTUAL INSURANCE COMPANY, CLEARFIELD INSURANCE LIMITED, THE COLLEGE/UNIVERSITY INSURANCE COMPANY, COLUMBIA MUTUAL INSURANCE COMPANY, COMMERCIAL STANDARD INSURANCE COMPANY, CONSOLIDATED MUTUAL INSURANCE COMPANY, COTTON STATES MUTUAL INSURANCE COMPANY, DRUGGISTS MUTUAL INSURANCE COMPANY, ELITE INSURANCE COMPANY, EMPLOYERS CASUALTY COMPANY, EMPLOYERS MUTUAL LIABILITY INS. CO. OF WISCONSIN, EXCHANGE MUTUAL INSURANCE COMPANY, FARMERS HOME MUTUAL INSURANCE COMPANY, FARMERS MUTUAL HAIL INS. CO. OF COLUMBIA, MO., FEDERATED MUTUAL INSURANCE COMPANY, FINANCIAL FIRE & CASUALTY COMPANY, FREMONT MUTUAL INSURANCE COMPANY, GENERAL FIRE & CASUALTY COMPANY, GRINNEL MUTUAL REINSURANCE CORPORATION, THE HAMILTON MUTUAL INSURANCE CO. OF CINCINNATI, HARFORD MUTUAL INSURANCE COMPANY, THE HARTFORD STEAM BOILER INSPECTION & INS. CO., HAWAIIAN INSURANCE & GUARANTY CO., LTD., HINGHAM MUTUAL FIRE INSURANCE COMPANY, INDEPENDENT FIRE INSURANCE COMPANY, INTEGRITY INSURANCE COMPANY, INTEGRITY MUTUAL INSURANCE COMPANY, INTERBORO MUTUAL INDEMNITY INSURANCE COMPANY, INTERSTATE INSURANCE COMPANY, IOWA MUTUAL INSURANCE COMPANY, IOWA NA-

TIONAL MUTUAL INSURANCE COMPANY, LIBERTY MUTUAL INSURANCE COMPANY, MANCHESTER INSURANCE & INDEMNITY COMPANY, MANUFACTURERS & MERCHANTS MUTUAL INS. CO., MERCHANTS MUTUAL INSURANCE COMPANY, MERRIMACK MUTUAL FIRE INSURANCE COMPANY, MFA MUTUAL INSURANCE COMPANY, MICHIGAN MILLERS MUTUAL INSURANCE COMPANY, MIDDLESEX MUTUAL ASSURANCE COMPANY, MIDDLESEX MUTUAL INSURANCE COMPANY, MIDLAND INSURANCE COMPANY, MIDLAND UNION INSURANCE COMPANY, MILBANK MUTUAL INSURANCE COMPANY, THE MILLERS MUTUAL FIRE INS. CO. OF TEXAS, THE MONARCH INSURANCE COMPANY OF OHIO, MORRISON ASSURANCE COMPANY, INC., THE MUTUAL FIRE, MARINE & INLAND INSURANCE CO., NEW HAMPSHIRE INSURANCE COMPANY, NORTH EAST INSURANCE COMPANY, OLD GUARD MUTUAL INSURANCE COMPANY, OLD RELIABLE FIRE INSURANCE COMPANY, OREGON MUTUAL INSURANCE COMPANY, PENNSYLVANIA MANUFACTURERS ASSOC. INS. .CO., PENNSYLVANIA MILLERS MUTUAL INSURANCE COMPANY, PHILADELPHIA MANUFACTURERS MUTUAL INS. CO., PROTECTION MUTUAL INSURANCE COMPANY, THE PROVIDENCE MUTUAL FIRE INSURANCE COMPANY, PUBLIC SERVICE MUTUAL INSURANCE COMPANY, RURAL MUTUAL INSURANCE COMPANY, SASKATCHEWAN GOVERNMENT INSURANCE OFFICE, SECURITY INSURANCE COMPANY OF HARTFORD, THE SHELBY MUTUAL INSURANCE CO. OF SHELBY, OHIO, STATE AUTOMOBILE MUTUAL INSURANCE COMPANY, STATE FARM FIRE & CASUALTY COMPANY, STONEWALL INSURANCE COMPANY, THE SUSSEX MUTUAL INSURANCE COMPANY, THOMAS JEFFERSON INSURANCE COMPANY, TRANS-NATIONAL INSURANCE

COMPANY, TRINITY UNIVERSAL INSURANCE COMPANY, UNION INSURANCE COMPANY, UNITED AMERICA INSURORS, UNITED FARM BUREAU MUTUAL INSURANCE COMPANY, UTAH HOME FIRE INSURANCE COMPANY, UTICA MUTUAL INSURANCE COMPANY, WEST BEND MUTUAL INSURANCE COMPANY, WESTERN NATIONAL MUTUAL INSURANCE COMPANY, WILSHIRE INSURANCE COMPANY, WISCONSIN FARMERS MUTUAL INSURANCE COMPANY, YOSEMITE INSURANCE COMPANY, by its attorneys, HINSHAW, CULBERTSON, MOELMANN, HOBAN & FULLER, and complaining of the defendant, CALVERT FIRE INSURANCE COMPANY, states onto the Court as follows:

1. Plaintiff is a corporation duly organized and existing under and by virtue of the laws of the State of Illinois, and at all times mentioned herein, was in the business of reinsuring property and casualty risks and organizing and managing a reinsurance pool consisting of property and casualty insurance companies herein above identified.

2. Defendant, CALVERT FIRE INSURANCE COMPANY, is a corporation licensed to do business by virtue of the laws of the State of Illinois, and at all times mentioned herein, was in the business of writing property and casualty insurance and participating in various reinsurance pools and arrangements.

3. Pursuant to plaintiff's business as a reinsurer of risks, numerous property and casualty insurance companies offer portions of risks from property and casualty insurance policies to plaintiff.

4. The aforesaid insurance companies thereby take advantage of the initial benefits of plaintiff's reinsurance program by reinsuring portions of insurance policies with plaintiff, and, as consideration therefore, plaintiff is paid a portion of the premium charged for such policies.

5. In return for the possibility of realizing an underwriting profit, plaintiff reinsures and accepts the aforesaid portions of risks and premiums which were originally accepted by the property and casualty insurance companies through sales of insurance policies.

6. Plaintiff's acceptance of portions of risks from the original vendors of property and casualty insurance policies is by written reinsurance contract, committing plaintiff to share in their losses which occur while such reinsurance contracts are in force.

7. As a form of risk-assuming activity in the hope of profit, various property and casualty insurance companies participate in plaintiff's reinsurance pool.

8. The aforesaid participants share in plaintiff's reinsurance pool by accepting portions of the risks and premiums assumed by plaintiff under its reinsurance contract.

9. Pursuant to the aforesaid arrangement, defendant, CALVERT FIRE INSURANCE COMPANY, a corporation, entered into a written agreement with the plaintiff, a copy of said agreement being attached hereto and incorporated herein as plaintiff's Exhibit "A".

10. The duration of the aforesaid agreement is found in Paragraph Ten thereof;

> "TERM
>
> This agreement shall apply to all contracts written or renewed by the company to become effective on or after January 1, 1974, and shall remain in force continuously until terminated at the close of any December 31 by either party giving to the other six months' prior notice in writing. However, in the event of such termination the Participant shall remain liable hereunder for its share of losses and expenses resulting from losses or occurrences which happen prior to such termination."

11. On April 22, 1974, defendant requested termination of the aforesaid agreement pursuant to letter and telegram, copies

of said documents being attached hereto and incorporated herein as plaintiff's Exhibit "B" and "C", respectively.

12. Plaintiff has agreed to terminate the aforesaid agreement at its earliest possible termination date, December 31, 1974, and has repeatedly requested that defendant honor the contractual obligations assumed by the defendant for the period from January 1, 1974, through December 31, 1974, pursuant to letters, copies of which are attached hereto and incorporated herein as plaintiff's Exhibits "D" and "E", respectively.

13. Defendant contends it is not bound by any portion of the aforesaid agreement by reason of its telegram, Exhibit "C", requesting retro-active termination and for other reasons unknown to plaintiff.

14. Plaintiff contends defendant is bound by the aforesaid agreement for the minimum participation period provided, i.e. January 1, 1974, through December 31, 1974, and that defendant must participate in premiums and losses attributable to the aforesaid period.

15. An actual controversy exists between the plaintiff and the defendant, and by the terms and provisions of Section 57.1 of the Civil Practice Act of the State of Illinois, this Court is invested with the power to declare the rights and liabilities of the parties hereto; and to give such other further relief as may be necessary in the premises.

WHEREFORE, the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, Individually, and for the use of 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool, prays:

1. That this Court determine and adjudicate the rights and liabilities of the parties hereto with respect to the reinsurance participating agreement herein above described and attached as plaintiff's Exhibit "A".

2. That this Court find and declare that the aforesaid agreement entered into between plaintiff and defendant is in full

force and effect between the parties, and that the defendant is obligated to participate in premiums and losses as set forth in the agreement between the plaintiff and the defendant attributable to the period of January 1, 1974, through December 31, 1974.

3. That this Court grant such other and further relief as it deems fit and proper under the evidence and circumstances.

HINSHAW, CULBERTSON, MOELMANN,
HOBAN & FULLER

By: /s/ THOMAS M. HAMILTON, JR.
Attorneys for the Plaintiff

69 West Washington Street—Suite 2700
Chicago, IL 60602
630-4400

Exhibit "A"

MULTIPLE LINE
REINSURANCE PARTICIPATING AGREEMENT

An Agreement of reinsurance between the AMERICAN MUTUAL REINSURANCE COMPANY, Chicago, Illinois, (hereinafter called the "Company") and

CALVERT FIRE INSURANCE COMPANY
Philadelphia, Pennsylvania

(hereinafter called the "Participant").

Whereas the Company issues to insurance companies (hereinafter called individually as an "Insurer") contracts and binders of reinsurance covering Property and Casualty lines of insurance and combinations thereof, and

Whereas the Company desires to reinsure with the Participant a share of liability under each of such contracts and binders of reinsurance.

Now therefore the Company agrees to cede and the Participant agrees to accept a share of liability under each such contract.

1. LIABILITY OF PARTICIPANT

   The Participant's share of each contract shall be the proportion which the capacity extended by the Participants to the Company bears to the total capacity extended by all Participants in such contract; provided that the liability of the Participant under this agreement for each loss or occurance shall be limited to $300,000 or to 7.5 per cent of the Company's liability under the applicable insurance contract, whichever is less.

2. ATTACHMENT OF LIABILITY

   The Participant's liability shall attach simultaneously with that of the Company. Property lines shall not exceed fifty per cent of the Company's total capacity.

3. FULL REINSURANCE CLAUSE

   Reinsurance under this agreement shall be subject to the same risks, terms, conditions and stipulations as may apply to the contracts issued by the Company, except as otherwise provided herein.

4. LOSS SETTLEMENTS

   A. The Company shall notify the Participant of any loss likely to involve the Participant on a quarterly basis.

   B. All loss settlements made by the Company shall be binding on the Participant which agrees to pay amounts for which it may be liable immediately upon being informed by the Company of the amount due or to be due.

   C. The Participant shall be liable for its share of all allocable expenses incurred by the Company in connection with the investigation, adjustment or litigation of claims or losses.

   D. All salvage or recoveries received subsequent to a loss settlement under this agreement shall be applied as if received prior to said loss settlement and all necessary adjustments shall be made between the Company and the Participant as soon as practicable following the receipt by the Company of such salvage or recoveries.

5. PREMIUM COMPUTATION AND PAYMENT

   A. The premium for this reinsurance shall be 95½% of the Participant's proportionate share of the earned premiums paid by the Company on the contracts reinsured hereunder less any premium adjustments paid by the Company on such contracts, and any premiums for reinsurance, if any, secured by the Company for the common account of all Participants.

   B. As soon as practicable after the close of each accounting period the Company shall send the Participant a report showing:

(1) The net total for the accounting period of the Participant's portions of:

(a) Contract premiums or return premiums received or paid by the Company,

(b) Premium adjustment paid or received by the Company,

(c) Premiums for reinsurance, if any, secured by the Company for the common account of all Participants,

(2) The computation of the reinsurance premium or return premium due to, or due from, the Participant for the accounting period.

C. The reinsurance premium due to the Participant or the ceded reinsurance return premium due to the Company shall be paid by the debtor to the creditor within 90 days after the close of the accounting period.

It is mutually agreed between the parties hereto, including their successors, liquidators and assigns, that the right to set off for any unpaid sums or accounts due between the Company and the Participant shall be binding on both parties.

6. EXCLUSIONS

A. No Atomic Energy or Nuclear Risk or Hazard insurance policies of Liability or Property lines which fall within the scope of coverage afforded by Mutual Atomic Energy Reinsurance Pool or Nuclear Energy Liability Insurance Pool or Nuclear Energy Property Insurance Pool shall be subject to contracts of the Company reinsured by this agreement.

B. War Risk

No liability shall attach hereunder in respect of any loss or damage on property insurance contracts which

is occasioned by enemy attack by armed forces, including action taken by military, naval or air force in resisting an actual or an immediately impending enemy attack; invasion; insurrection; rebellion; revolution; civil war; usurped power or confiscation by order of any government or public authority, but this shall not be construed as relieving the Participant of liability, provided it would otherwise have been liable hereunder for loss or damage which would be recoverable under:

(1) A standard fire policy or standard extended coverage endorsement, or other standard policy (containing a standard war exclusion clause) as extended civil authority clause, or

(2) Any vandalism and malicious mischief endorsement authorized by the Explosion Conference or other regulatory body having jurisdiction, or under similar endorsements not broader in scope than such authorized endorsements.

7. COMPANY NON-ASSESSABLE

The Company shall not be a member of or subject to the by-laws of the Participant, or be subject to any liability for assessment.

8. ERRORS AND OMISSIONS

Delays, errors and omissions inadvertently made under this agreement shall not invalidate the liability of either party.

9. INSPECTION OF BOOKS AND RECORDS

The Participant or its duly authorized representative shall have the right, at any reasonable time, to examine at the office of the Company any books, documents, reports or records which pertain directly to the subject matter of this agreement.

10. TERM

This agreement shall apply to all contracts written or renewed by the Company to become effective on or after January 1, 1974 and shall remain in force continuously until terminated at the close of any December 31, by either party giving to the other 6 months' prior notice in writing. However, in the event of such termination the Participant shall remain liable hereunder for its share of losses and expenses resulting from losses or occurrences which happen prior to such termination.

11. ARBITRATION

In the event of any irreconcilable dispute between the Company and the Participant in connection with this agreement, such dispute shall be submitted to a Board of Arbitration for arbitration.

The Board of Arbitration shall consist of one arbitrator to be chosen by the Company and one arbitrator to be chosen by the Participant, and, an umpire to be chosen as promptly as possible by the two arbitrators. If the two arbitrators are unable to agree upon an umpire, each arbitrator shall name three candidates, two of whom shall be declined by the other arbitrator and the choice shall be made between the two remaining candidates by drawing lots. The arbitrators and umpire shall be disinterested executive officers of casualty insurance companies authorized to transact business in the United States. The arbitrators are relieved from all judicial formalities and may abstain from following the strict rules of evidence. The decision of the arbitrators shall be final and binding upon both the Company and the Participant, but failing to agree they shall call in the umpire and the decision of the majority shall be final and binding upon both the Company and the Participant.

The Company and the Particpants shall bear the expense of its own arbitrator and shall jointly and equally bear with

the other the expense of the umpire and of the arbitration. Any arbitration shall take place in Chicago, Illinois, unless otherwise mutually agreed.

As soon as either the Company or the Participant demands arbitration and has named an arbitrator, the other binds itself to name an arbitrator within one month thereafter. The Company and the Participant shall submit their cases to the arbitrators within one month after selection of the umpire. The arbitrators are empowered, however, to extend the time granted in which to submit cases for a further period of not more than 30 days.

12. INSOLVENCY

The reinsurance provided by each and every reinsurance contract heretofore or hereafter entered into by and between the parties hereto shall be payable by the Participant directly to the Company or its liquidator, receiver or statutory successor on the basis of the liability of the Company under the contract or contracts reinsured without diminution because of the insolvency of the Company. In the event of the insolvency of the Company, the liquidator or receiver or statutory successor of the Company shall give written notice of the pendency of each claim against the Company on a contract reinsured within a reasonable time after such claim is filed in the insolvency proceeding; and during the pendency of such claim, the Participant may investigate such claim and interpose, at its own expense, in the proceeding where such claim is to be adjudicated any defense or defenses which it may deem available to the Company, its liquidator or receiver or statutory successor. The expense thus incurred by the Participant shall be chargeable, subject to court approval, against the Company as part of the expense of liquidation to the extent of such proportionate share of the benefit as shall accrue to the Company solely as a result of the defense undertaken

by the Participant. The reinsurance shall be payable as hereinbefore in this paragraph provided except as otherwise provided by Section 315 (relating to Fidelity and Surety Risks) of the Insurance Law of New York except (a) where the contract specifically provides another payee of such reinsurance in the event of the insolvency of the Company and (b) where the Participant with the consent of the direct insured or insureds has specifically assumed in writing such policy obligations of the Company as direct obligations of the Participant to the payees under such policies and in substitution for the obligations of the Company to such payees.

Executed, in duplicate, at Chicago, Illinois, as of this 11th day of January 1974.

AMERICAN MUTUAL REINSURANCE COMPANY
By /s/ W. E. WINTER
Pres.

CALVERT FIRE INSURANCE COMPANY
By /s/ G. E. ROBERTS
Pres.

APPENDIX B

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
County Department, Law Division

AMERICAN MUTUAL REINSURANCE COMPANY, individually and for the use of 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool, *Plaintiff,* *vs.* CALVERT FIRE INSURANCE COMPANY, *Defendant.*	No. 74 L 10737 Extraordinary Remedy

ANSWER AND COUNTERCLAIM

Now comes the defendant, CALVERT FIRE INSURANCE COMPANY ("Calvert"), by its attorney, Michael L. Weissman of Aaron, Aaron, Schimberg & Hess, and as and for its answer to the Complaint for Declaratory Judgment ("Complaint") filed herein by AMERICAN MUTUAL REINSURANCE COMPANY ("AMRECO"), individually and for the use of 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool, states as follows:

1. Calvert admits that AMRECO is in the business of reinsuring property and casualty risks and organizing and managing a reinsurance pool consisting of property and casualty insurance companies but is without knowledge or information sufficient to form a belief as to the truth of the remaining allegations set forth in Paragraph 1 of the Complaint.

2. Calvert admits the allegations set forth in Paragraph 2 of the Complaint.

3. Calvert admits the allegations set forth in Paragraph 3 of the Complaint.

4. Calvert is without knowledge or information sufficient to form a belief as to the truth of the allegations set forth in Paragraph 4 of the Complaint.

5. Calvert admits the allegations set forth in Paragraph 5 of the Complaint.

6. Calvert is without knowledge or information sufficient to form a belief as to the truth of the allegations set forth in Paragraph 6 of the Complaint.

7. Calvert admits the allegations set forth in Paragraph 7 of the Complaint.

8. Calvert admits the allegations set forth in Paragraph 8 of the Complaint.

9. Calvert admits that it executed the written agreement attached to AMRECO's Complaint as Exhibit "A" but, answering further, Calvert states that it was induced to execute said written agreement by reason of material misrepresentations of fact and the failure to state material facts necessary to make the statements made, in light of the circumstances under which they were made, not misleading thus rendering the said agreement void *ab initio.*

10. Calvert admits that Paragraph Ten of the written agreement described in Paragraph 9 of the Complaint (hereinafter referred to as the "reinsurance participation agreement") contains the provisions set forth in Paragraph 10 of the Complaint but denies the remaining allegations set forth in Paragraph 10 of the Complaint.

11. Calvert admits the allegations set forth in Paragraph 11 of the Complaint.

12. Calvert admits that AMRECO has refsued to terminate the reinsurance participation agreement as of January 1, 1974 but denies all of the remaining allegations set forth in Paragraph 12 of the Complaint.

13. Calvert admits the allegations set forth in Paragraph 13 of the Complaint.

14. Calvert admits that AMRECO contends that Calvert is bound by the reinsurance participation agreement through December 31, 1974 but denies all of the remaining allegations set forth in Paragraph 14 of the Complaint.

15. Calvert admits that a controversy exists between it and AMRECO but denies all of the remaining allegations set forth in Paragraph 15 of the Complaint.

FIRST AFFIRMATIVE DEFENSE

1. The participatory interest in the 1974 AMRECO Multiple Line Pool which AMRECO offered and sold to Calvert on or about January 11, 1974 and which AMRECO offered and sold to more than 90 other insurance companies, constituted an offer and sale to the public of a security within the meaning of Section 2(1) and 5 of the Securities Act of 1933, as amended (the "1933 Act").

2. Said security was not registered in violation of the registration requirements of Section 5 of the 1933 Act.

3. At no time were the offerees and purchasers of said security provided with information equivalent to that which would have been available to them had a prospectus in accordance with Section 5 of the 1933 Act been prepared and delivered to them at the time of the offer and sale.

4. On January 9, 1975, Calvert delivered a notice of rescission to AMRECO, both individually and as agent for the 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool and tendered any and all interest it had acquired in the aforesaid security. Said notice is attached hereto as Exhibit "A" and made a part hereof.

5. AMRECO has refused to accept the foregoing tender.

6. The failure of AMRECO to register said security entitles Calvert to rescission pursuant to Section 12(1) of the 1933 Act.

SECOND AFFIRMATIVE DEFENSE

1. The participatory interest in the 1974 AMRECO Multiple Line Pool offered and sold to Calvert by AMRECO constituted the offer and sale of a security within the meaning of Section 3(a)(10) of the Securities and Exchange Act of 1934, as amended (the "1934 Act").

2. In connection with the offer and sale of said security to Calvert, AMRECO, by the use of the mails and other means and instrumentalities of interstate commerce, has (1) employed devices, schemes and artifices to defraud; (2) made untrue statements of material fact and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (3) engaged in acts, practices and a course of business which have operated as a fraud and deceit upon Calvert in violation of Section 10(b) of the 1934 Act and Rule 10b-5 promulgated thereunder.

3. On January 9, 1975, Calvert delivered a notice of rescission to AMRECO, both individually and as agent for the 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool and tendered any and all interest it had acquired in the aforesaid security.

4. AMRECO has refused to accept the foregoing tender.

5. As a result of the foregoing omissions and misrepresentations of material fact, Calvert has suffered substantial injury and is entitled to rescission of its purchase of the aforesaid security.

THIRD AFFIRMATIVE DEFENSE

1. The participatory interest in the 1974 AMRECO Multiple Line Pool offered and sold to Calvert on or about January 11, 1974 by AMRECO constituted the offer and sale of a security within the meaning of Section 137-2.1 of the Illinois Securities Law of 1953, as amended (the "Illinois Securities Law"), Ill.

Rev.Stat. ch. 121½, §137-2.1, and Rule 130 promulgated thereunder.

2. In connection with the offer and sale of said security to Calvert, AMRECO has made untrue statements of material fact and omitted to state facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading in violation of Section 137.12(G) of the Illinois Securities Law.

3-4. Calvert hereby realleges and incorporates by reference Paragraphs 3 and 4 of its Second Affirmative Defense as Paragraphs 3 and 4 of its Third Affirmative Defense as though set forth fully herein.

5. Notice of Calvert's election to rescind was given in compliance with Section 137.13(B) of the Illinois Securities Law.

6. As a result of the foregoing omissions and misrepresentations of material fact, Calvert is entitled to rescission of its purchase of the aforesaid security.

FOURTH AFFIRMATIVE DEFENSE

1. The participatory interest in the 1974 Multiple Line Pool offered and sold to Calvert on January 11, 1974 by AMRECO constitutes the offer and sale of a security within the meaning of Section 26(a)(5) of the Maryland Securities Act, as amended ("Maryland Securities Act"), Md. Code Ann. art. 32A, §26(a)(5).

2. In connection with the offer and sale of said security to Calvert, AMRECO has made untrue statements of material fact and omitted to state facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading in violation of Section 34(a)(2) of the Maryland Securities Act, as more fully described hereinafter.

3. As a result of the foregoing omissions and misrepresentations of material fact, Calvert has been substantially injured and

is entitled to damages pursuant to Section 34(a)(2) of the Maryland Securities Act.

FIFTH AFFIRMATIVE DEFENSE

1. In order to induce Calvert to enter into reinsurance participation agreement, AMRECO, through its agents, including one Robert Morris, made material misrepresentations of fact to Calvert concerning the 1974 AMRECO Multiple Line Pool.

2. In reliance on AMRECO's material misrepresentations of fact, Calvert executed the reinsurance participation agreement on or about January 11, 1974.

3. Had Calvert known that the foregoing representations were false, it would not have signed said reinsurance participation agreement.

4. As a result of the foregoing material misrepresentations of fact, Calvert has been substantially injured.

SIXTH AFFIRMATIVE DEFENSE

1. By the pleadings filed in this cause, AMRECO purports to act as agent for the members of the unincorporated association known as the 1974 AMRECO Multiple Line Pool.

2. The only agreements executed by the members of the 1974 AMRECO Multiple Line Pool were identical to the agreement annexed to AMRECO's Complaint as Exhibit "A" and said agreement does not confer authority upon AMRECO to maintain any suit or proceeding on behalf of the members of the 1974 AMRECO Multiple Line Pool.

3. Since AMRECO is without authority to institute this action, its Complaint must be stricken and this action dismissed.

SEVENTH AFFIRMATIVE DEFENSE

AMRECO participated in and managed the 1974 AMRECO Multiple Line Pool without obtaining the approval of the Illinois Department of Insurance in violation of 73 Ill. Rev. Stat. §786.

WHEREFORE, defendant CALVERT FIRE INSURANCE COMPANY prays that this Court enter judgment in its favor against AMERICAN MUTUAL REINSURANCE COMPANY and that costs be taxed to AMERICAN MUTUAL REINSURANCE COMPANY.

COUNTERCLAIM

As and for its Counterclaim to the said Complaint for Declaratory Judgment, Calvert states as follows:

COUNT ONE

1. The participatory interest in the 1974 AMRECO Multiple Line Pool which AMRECO offered and sold to Calvert on or about January 11, 1974 and which AMRECO offered and sold to more than 90 other insurance companies, constituted an offer and sale to the public of a security within the meaning of Sections 2(1) and 5 of the Securities Act of 1933, as amended (the "1933 Act").

2. Said security was not registered in violation of the registration requirements of Section 5 of the 1933 Act.

3. At no time were the offerees and purchasers of said security provided with information equivalent to that which would have been available to them had a prospectus in accordance with Section 5 of the 1933 Act been prepared and delivered to them at the time of the offer and sale.

4. On January 9, 1975, Calvert delivered a notice of rescission to AMRECO, both individually and as agent for the 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool and tendered any and all interest it had acquired in the aforesaid security.

5. AMRECO has refused to accept the foregoing tender.

6. The failure of AMRECO to register said security entitles Calvert to rescission pursuant to Section 12(1) of the 1933 Act.

WHEREFORE, defendant CALVERT FIRE INSURANCE COMPANY prays that this Court enter an order declaring that Calvert's purchase of the aforesaid security was null and void and that this Court grant such other and further relief as it shall deem equitable and appropriate.

COUNT TWO

1. The participatory interest in the 1974 AMRECO Multiple Line Pool offered and sold to Calvert on or about January 11, 1974 by AMRECO constituted the offer and sale of a security within the meaning of Section 137-2.1 of the Illinois Securities Law of 1953, as amended (the "Illinois Securities Law"), Ill. Rev. Stat. ch. 121½, §137-2.1, and Rule 130 promulgated thereunder.

2. In connection with the offer and sale of said security to Calvert, AMRECO has made untrue statements of material fact and omitted to state facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading in violation of Section 137.12(G) of the Illinois Securities Law.

3. On January 9, 1975, Calvert delivered a notice of rescission to AMRECO, both individually and as agent for the 99 property and casualty insurance companies who are participants in the 1974 AMRECO Multiple Line Pool and tendered any and all interest it had acquired in the aforesaid security.

4. AMRECO has refused to accept the foregoing tender.

5. Notice of Calvert's election to rescind was given in compliance with Section 137.13(B) of the Illinois Securities Law.

6. As a result of the foregoing omissions and misrepresentations of material fact, Calvert is entitled to rescission of its purchase of the aforesaid security.

WHEREFORE, defendant CALVERT FIRE INSURANCE COMPANY prays that this Court enter an order declaring that Calvert's purchase of the aforesaid security was null and void

and that this Court grant such other and further relief as it shall deem equitable and appropriate.

COUNT THREE

1. The participatory interest in the 1974 Multiple Line Pool offered and sold to Calvert on January 11, 1974 by AMRECO constitutes the offer and sale of a security within the meaning of Section 26(a)(5) of the Maryland Securities Act, as amended ("Maryland Securities Act"), Md. Code Ann. art. 32A, §26(a)(5).

2. In connection with the offer and sale of said security to Calvert, AMRECO has made untrue statements of material fact and omitted to state facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading in violation of Section 34(a)(2) of the Maryland Securities Act.

3. As a result of the foregoing omissions and misrepresentations of material fact, Calvert has been substantially injured and is entitled to damages pursuant to Section 34(a)(2) of the Maryland Securities Act.

WHEREFORE, defendant CALVERT FIRE INSURANCE COMPANY prays that this Court award damages against AMERICAN MUTUAL REINSURANCE COMPANY in the amount of Two Million Dollars ($2,000,000.00) and grant such other and further relief as this Court may deem equitable and appropriate.

COUNT FOUR

1. In order to induce Calvert to enter into the reinsurance participation agreement, AMRECO, through its agents, including one Robert Morris, made material misrepresentations of fact to Calvert concerning the 1974 AMRECO Multiple Line Pool.

2. In reliance on AMRECO's material misrepresentations of fact, Calvert executed the reinsurance participation agreement on or about January 11, 1974.

3. Had Calvert known that the foregoing representations were false, it would not have signed said reinsurance participation agreement.

4. As a result of the foregoing material misrepresentations of fact, Calvert has been substantially injured.

WHEREFORE, defendant CALVERT FIRE INSURANCE COMPANY prays that this Court award damages against AMERICAN MUTUAL REINSURANCE COMPANY in the amount of Two Million Dollars ($2,000,000.00) and grant such other and further relief as this Court may deem equitable and appropriate.

CALVERT FIRE INSURANCE COMPANY
By /s/ MICHAEL L. WEISSMAN
Its Attorney

Michael L. Weissman
Aaron, Aaron, Schimberg & Hess
One First National Plaza
Chicago, Illinois 60603
(312) 236-8552

CALVERT FIRE INSURANCE COMPANY
300 St. Paul Place
Baltimore, Maryland 21202

January 9, 1975

American Mutual Reinsurance Company,
individually and as agent for the
property and casualty insurance
companies which are participants
in the 1974 AMRECO Multiple Line
Pool,

One East Wacker Drive
Chicago, Illinois 60601

Attention: Mr. Wallace E. Winter, President

NOTICE OF RESCISSION

Gentlemen:

Pursuant to the applicable provisions of the Securities Act of 1933, as amended, the Securities Exchange Act of 1934, as amended, and the Illinois Securities Act of 1953, the undersigned corporation hereby elects to rescind the purchase of the security which it made from you on January 11, 1974 effective as of January 1, 1974 as per our telegram to you dated April 19, 1974 and our letter to you dated April 22, 1974. We tender to you herewith any interest which we acquired in the security, i.e., our participation in the 1974 AMRECO Multiple Line Pool.

The exercise of the right of rescission is without prejudice to any claim for damages we have under common law or federal or state securities laws.

Yours very truly,

CALVERT FIRE INSURANCE COMPANY
/s/ MICHAEL L. WEISSMAN
Its Attorney

RECEIPT ACKNOWLEDGED:
this 9th day of January, 1975.

AMERICAN MUTUAL REINSURANCE COMPANY

By: .....

APPENDIX C

STATE OF ILLINOIS } ss.
COUNTY OF COOK }

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
County Department, Law Division

AMERICAN MUTUAL REINSURANCE CO., *Plaintiff,*
vs.
CALVERT FIRE INSURANCE CO., *Defendant.* — No. 74 L 10737

REPORT OF PROCEEDINGS had at the hearing of the above-entitled cause before the Honorable Arthur L. Dunne, one of the Judges of said Court on the 6th day of June A. D., 1975.

Present:

Mr. Thomas J. Weithers, Mr. Thomas M. Hamilton, appeared on behalf of the Plaintiff;

Mr. Michael Weissman, Mr. Don Shapiro, appeared on behalf of the Defendant.

* * * * *

(pp. 63-64)

Based upon my opinion of the record, the briefs, the transcript and the arguments, it appears that the principal test, which is applied by the upper courts in the resolving of this very thorny issue, is whether or not—Strike that. Is a consideration of the nature of the transaction and the capacity of the parties dealing therein.

Accordingly, I further find, again, unfortunately at the risk of oversimplification, that the issue is simply this, whether or not the right to participate in the profits and to share the losses of this organization constitutes a security interest within the meaning of the applicable State and Federal statutes. I specifically find that it does not. That is my ruling.

* * * * *

APPENDIX D

STATE OF ILLINOIS }
COUNTY OF COOK } ss.

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
County Department, Law Division

AMERICAN MUTUAL REINSURANCE COMPANY, etc.,
Plaintiff,
vs.
CALVERT FIRE INSURANCE COMPANY,
Defendant.
No. 74 L 10737

ORDER STRIKING FIRST, SECOND, THIRD, FOURTH AND SIXTH AFFIRMATIVE DEFENSES

THIS CAUSE COMING TO BE HEARD on motion of the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, for leave of court to file its motion to strike the First, Second, Third, Fourth and Sixth Affirmative Defenses of the defendant, and further, for leave of court to file its reply to the Fifth and Seventh Affirmative Defenses of the defendant's answer and further, for a hearing thereon, instanter, the court having read the briefs of parties with regard to the issues raised in defendant's Affirmative Defenses and, heard on arguments of counsel with regard to those issues on June 6, 1975, due notice having been given and the court being fully advised in the premises:

IT IS HEREBY ORDERED that leave be and the same is hereby granted the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, to file its motion to strike the First, Second, Third,

Fourth and Sixth Affirmative Defenses of the defendant, CALVERT FIRE INSURANCE COMPANY, and its reply to the Fifth and Seventh Affirmative Defenses instanter.

This court makes the following findings of fact with regard to the agreement entered into by the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, and the defendant, CALVERT FIRE INSURANCE COMPANY, on January 11, 1974.

1. That the said agreement does not constitute a "security" as that term has been defined by §1(1) of the Securities Act of 1933.
2. That plaintiff's business of obtaining reinsurance contracts constitutes the carrying on of the "business of insurance".
3. That AMERICAN MUTUAL REINSURANCE COMPANY's contract does not constitute a "security" as defined by §137-2.1 of Illinois Securities Law of 1933 as amended (the "Illinois Securities Law"), Illinois Revised Statutes §121½ and 137½ and Rule 130 promulgated thereunder.
4. That AMERICAN MUTUAL REINSURANCE COMPANY's contract does not constitute a "security" as defined in §26(a)(5) of the Maryland Securities Act as amended ("Maryland Securities Act") Maryland Code Annotated Acts 32(a) §26(a)(5)
5. That plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, properly brings this cause of action as a declaratory judgment action in this court.

Pursuant to the above findings of fact, this court makes the following conclusions of law with regard to the agreement entered into between the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, and the defendant, CALVERT FIRE INSURANCE COMPANY on January 11, 1974:

1. The McCarren-Ferguson Act, 15 U.S.C.A. §1101-1105, precludes the application of the Securities Act of 1933 to the "business of insurance" when that business is subject to regulation by a state.

2. That CALVERT FIRE INSURANCE COMPANY was not, as a matter of law, a purchaser of a security but rather a seller of reinsurance contracts.
3. That the American Mutual Reinsurance Company's contract with Calvert is exempt from registration under §3(a)(8) of the Securities Act of 1933.
4. That the McCarren-Ferguson Act, 15 U.S.C.A. §1101-1105, precludes the application of the Securities Exchange Act of 1934 to the said agreement between the parties.
5. AMERICAN MUTUAL REINSURANCE COMPANY's reinsurance contract does not constitute a "security" as defined by §137.2.1 of the Illinois Securities Law of 1953 as amended ("Illinois Securities Law") Illinois Revised Statute, Chap. 121½ §137.2.1 and Rule 130 promulgated thereunder.
6. That the AMERICAN MUTUAL REINSURANCE COMPANY's reinsurance contract does not constitute a "security" as defined by §26(a)(5) of the Maryland Securities Act as amended ("Maryland Securities Act"), Maryland Code Annotated Act 32A §26(a)(5).
7. That the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, properly brings this action as a declaratory judgment action.

Pursuant to the above findings of fact and conclusions of law, it is hereby ordered that the First, Second, Third, Fourth and Sixth Affirmative Defenses of the defendant, Calvert Fire Insurance Company, be and the same are hereby stricken.

Enter ARTHUR L. DUNNE
Judge

June 16, 1975

HINSHAW, CULBERTSOM, MOELMANN,
HOBAN & FULLER
Attorneys for Plaintiff
69 West Washington Street
Chicago, Illinois 60602
630-4400

APPENDIX E

STATE OF ILLINOIS }
COUNTY OF COOK } ss.

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
County Department, Law Division

AMERICAN MUTUAL REINSURANCE COMPANY, etc., *Plaintiff,* *vs.* CALVERT FIRE INSURANCE COMPANY, *Defendant.*	No. 74 L 10737

ORDER DISMISSING COUNTS I, II AND III
OF DEFENDANT'S COUNTERCLAIM

THIS CAUSE COMING to be heard on motion of the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, for entry of an order dismissing Counts I, II and III of the counterclaim filed herein by Calvert Fire Insurance Company, pursuant to the hearing before this court on June 6, 1975, the court having reviewed the briefs filed herein by the respective parties, and having heard arguments of counsel, due notice having been given, and the court being fully advised in the premises and the court having ordered on June 6, 1975 the said counts of the defendant's counterclaim were dismissed;

THIS COURT MAKES THE FOLLOWING FINDINGS OF FACT with regard to the agreement entered into between the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, and the defendant, CALVERT FIRE INSURANCE COMPANY, on January 11, 1974:

1. That the said agreement does not constitute a "security" under the Securities Act of 1933.
2. That the said agreement does not constitute a "security" under the Securities Exchange Act of 1934.
3. That the said agreement does not constitute a "security" as defined by §137-2.1 of the Illinois Securities Law of 1953, as amended ("Illinois Securities Law") Illinois Revised Statute Chap. 121½ §137-2.1 and Rule 130 promulgated thereunder.
4. That the said agreement does not constitute a "security" as defined by 26(a)(5) of the Maryland Securities Act, as amended ("Maryland Securities Act") Maryland Code Annotated Act 32A §26(a)(5).

THIS COURT MAKES THE FOLLOWING CONCLUSIONS OF LAW with regard to the agreement entered into between the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY and the defendant, CALVERT FIRE INSURANCE COMPANY on January 11, 1974.

1. That the said agreement does not constitute a "security" under the Securities Act of 1933.
2. That the said agreement does not constitute a "security" under the Securities Act of 1934.
3. The McCarren-Ferguson Act, 15 U. S. C. A. §§1101-1105, precludes the application of the Securities Act of 1933 to the "business of insurance" when that business is subject to regulation by a state.
4. That CALVERT FIRE INSURANCE COMPANY was not, as a matter of law, a purchaser of a security but rather a seller of reinsurance contracts.
5. That American Mutual Reinsurance Company's contract is exempt from registration under §3(a)(8) of the Securities Act of 1933.
6. AMERICAN MUTUAL REINSURANCE COMPANY's reinsurance contract does not constitute "security" as defined by §137-2.1 of the Illinois Securities Law of 1953 as amended ("Illinois Securities Law") Illinois Revised Statute, Chap. 121½ §137-2.1 and Rule 130 promulgated thereunder.

7. That the American Mutual Reinsurance Company's reinsurance contract does not constitute a "security" as defined by §26(a)(5) of the Maryland Securities Act as amended ("Maryland Securities Act"), Maryland Code Annotated Act 32A §26(a)(5).

PURSUANT TO THE ABOVE FINDINGS OF FACT AND CONCLUSIONS OF LAW, this court orders that Counts I, II and III of the defendant's Counterclaim be and the same are hereby dismissed.

ENTER ARTHUR L. DUNNE
Judge

June 16, 1975

HINSHAW, CULBERTSON, MOELMANN,
HOBAN & FULLER
Attorneys for Defendant American Mutual
Reinsurance Co.
69 West Washington Street
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APPENDIX F

IN THE CIRCUIT COURT OF COOK COUNTY, ILLINOIS
County Department, Law Division

AMERICAN MUTUAL REINSURANCE COMPANY, *Plaintiff,* vs. CALVERT FIRE INSURANCE COMPANY, *Defendant.*	No. 74 L 10737

ORDER CERTIFYING QUESTIONS OF LAW FOR INTERLOCUTORY APPEAL

This cause coming on to be heard on the motions of the plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, to dismiss Counts I, II and III of the Counterclaim and to strike the First, Second, Third and Fourth Affirmative Defenses in the Answer of defendant, CALVERT FIRE INSURANCE COMPANY; the Court having reviewed the briefs filed herein by the respective parties, and having heard arguments of counsel, due notice having been given, and the Court being fully advised in the premises;

THE COURT HAVING ORDERED, that plaintiff's motion to dismiss Counts I, II and III of defendant's Counterclaim be granted; and

THE COURT HAVING FURTHER ORDERED, that plaintiff's motion to strike the First, Second, Third and Fourth Affirmative Defenses in defendant's Answer be granted;

The Court finds, under Rule 308 of the Rules of the Supreme Court of Illinois, that its ruling on Counts I, II and III of

defendant's Counterclaim and on the said First, Second, Third and Fourth Affirmative Defenses in defendant's Answer and the orders entered on June 16, 1975 involve questions of law as to which there is substantial grounds for difference of opinion and that an immediate appeal from this order may materially advance the ultimate termination of this litigation; and

The Court finds that the questions of law involved in the entry of this order are:

1. "Is the Multiple Line Reinsurance Participating Agreement dated January 11, 1974 between AMERICAN MUTUAL REINSURANCE COMPANY and CALVERT FIRE INSURANCE COMPANY (Exhibit 'A' hereto) in any respect a 'security' under the Securities Act of 1933, 15 U.S.C. 77(b)(1)?"
2. "Is the Multiple Line Reinsurance Participating Agreement dated January 11, 1974 between AMERICAN MUTUAL REINSURANCE COMPANY and CALVERT FIRE INSURANCE COMPANY (Exhibit 'A' hereto) in any respect a 'security' under the Securities Exchange Act of 1934, 15 U.S.C. 78c.(10)?"
3. "Does the McCarran-Ferguson Act, 15 U.S.C. 1101 et seq., preclude the application of the Securities Act of 1933 to the 'business of insurance' if that business is subject to state regulation?"
4. "When defendant, CALVERT FIRE INSURANCE COMPANY, entered into the Agreement which is annexed hereto as Exhibit 'A', did it simply sell reinsurance to plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, or did it also purchase a security from plaintiff?"
5. "Assuming that defendant, CALVERT FIRE INSURANCE COMPANY, purchased a security from plaintiff, AMERICAN MUTUAL REINSURANCE COMPANY, was such security exempted from registration under Section 3(a)(8) of the Securities Act of 1933?"
6. "Is the Multiple Line Reinsurance Participating Agreement dated January 11, 1974 between AMERICAN MUTUAL REINSURANCE COMPANY and CALVERT FIRE INSURANCE COMPANY (Exhibit 'A' hereto) in any respect a 'security' under the Illinois Securities Act of 1953, Chapter 121½ Ill. Rev. Stat. 137-2.1 and Rule 130 promulgated thereunder?"

7. "Is the Multiple Line Reinsurance Participating Agreement dated January 11, 1974 between AMERICAN MUTUAL REINSURANCE COMPANY and CALVERT FIRE INSURANCE COMPANY (Exhibit 'A' hereto) in any respect a 'security' under the Maryland Securities Act, 32A Md. Code Anno. 25(1)(5)?"

IT IS FURTHER ORDERED, that all proceedings in this Court shall be stayed pending final disposition of an application for leave to file an interlocutory appeal in the Illinois Appellate Court.

Dated: June 17, 1975.

ENTER: ARTHUR L. DUNNE
Judge

MICHAEL L. WEISSMAN
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APPENDIX G

62120 AMERICAN MUTUAL REINSURANCE COMPANY, an Illinois corporation, *Plaintiff-Counterdefendant-Appellee,* *v.* CALVERT FIRE INSURANCE COMPANY, a Pennsylvania corporation, *Defendant-Counterplaintiff-Appellant.*	APPEAL FROM THE CIRCUIT COURT OF COOK COUNTY. HONORABLE ARTHUR L. DUNNE, JUDGE PRESIDING.

Mr. JUSTICE LINN delivered the opinion of the court:

Plaintiff, American Mutual Reinsurance Company, (Amreco), brought suit for declaratory judgment against defendant, Calvert Fire Insurance Company (Calvert). In its suit, Amreco sought to have a contract of insurance entered into between the parties declared to be binding and in full force and effect. Calvert by way of answer and counterclaim alleged, *inter alia*, that the agreement constituted a sale of a security by Amreco and that, in connection with the sale, Amreco had violated federal and state securities laws. On that basis, Calvert sought rescission of the contract and an award of damages. The trial court struck and dismissed the several affirmative defenses and counts of the counterclaim which alleged violations of the securities laws. Pursuant to Supreme Court Rule 308, (Ill. Rev. Stat. 1973, ch. 110A, par. 308) the trial court certified questions of law for interlocutory appeal.

Amreco's complaint alleged that it is an Illinois corporation in the business of reinsuring property and casualty risks and organizing and managing a reinsurance pool comprised of one

hundred insurance companies.[1] Amreco undertakes to reinsure portions of property and casualty insurance policies issued by primary insurers to individual insurers, and in return receives a portion of the premiums paid for such policies. Calvert, an insurance company licensed to do business in Illinois, and the other insurance companies, participate in Amreco's insurance pool by accepting portions of the risks assumed by Amreco and receiving portions of the premiums earned. The agreement with Calvert, entitled "Multiple Line Participating Agreement," provides that Calvert's participation in this arrangement would commence January 1, 1974, and could be terminated by either party at the close of any December 31, by giving the other party 6 months prior written notice.

On April 22, 1974, Calvert requested 'retro-active termination" of the agreement. Amreco has maintained that Calvert is bound for the minimum participation period of one year. By this suit Amreco seeks to compel Calvert to share the premiums and losses attributable to that period.

In its answer, Calvert set forth seven affirmative defenses, five of which were claimed to entitle Calvert to rescission of the contract and an award of damages. The first defense alleged that the participatory interests in the pool which Amreco sold constituted an offer and sale to the public of a security within the meaning of the Securities Act of 1933 (15 U.S.C., §77a, *et seq.*) and that Amreco did not comply with the registration requirements of the Act. The second defense alleged violations of the Securities and Exchange Act of 1934 (15 U.S.C., §78a, *et seq.*) in that Amreco had made omissions and misrepresentations of material fact. The third and fourth defenses alleged violations of the securities laws of Illinois and Maryland. The fifth defense alleged common law fraud in that Amreco's agents made material misrepresentations of fact, upon which Calvert relied, resulting in injury to Calvert.

1. Suit was also brought for the use of the other insurance companies participating in the pool.

The sixth defense alleged that Amreco lacked authority to maintain a suit on behalf of the other participants, and the seventh defense alleged that Amreco participated in and managed the pool without obtaining the approval of the Illinois Department of Insurance.

Calvert's counterclaim was comprised of four counts. The first three counts alleged that Amreco's offer and sale to Calvert of the participatory interest constituted a security and violated the federal Securities Act of 1933, and the Illinois and Maryland securities laws, respectively. Calvert sought to have the purchase declared void and sought damages of two million dollars. The fourth count, seeking similar damages, alleged common law fraud by Amreco.

In its motion to strike the first, second, third, fourth and sixth defenses set forth in the answer, and to dismiss the first three counts of the counterclaim, Amreco alleged, *inter alia,* that its contract with Calvert did not constitute a security under federal, Illinois, and Maryland law. Further, Amreco alleged that the McCarren-Ferguson Act (15 U.S.C., §1011, *et. seq.*) precluded application of federal securities law, that the reinsurance contract was exempt from registration under section 3(a)(8) of the Securities Act of 1933, and that Calvert was a seller of reinsurance and not a purchaser of a security.

The trial court found that the agreement did not constitute a security and struck those portions of Calvert's answer and counterclaim containing such allegations. This interlocutory appeal followed. We affirm the result reached by the trial court.

At the outset we note that in determining the sufficiency of the answer and counterclaim when attacked by a motion to strike or dismiss, all well pleaded facts are taken as true. *(City of Chicago* v. *Loitz* (1975), 61 Ill. 2d 92, 329 N.E. 2d 208.) The disposition of the motions must be made upon a consideration of the allegations contained in Calvert's pleadings. *(Mutual Tobacco Co.* v. *Halpin* (1953), 414 Ill. 226, 111 N.E.2d 155.)

Although the parties have urged us to consider affidavits submitted by their corporate officers, they cannot properly be considered in determining the sufficiency of the pleadings. *Brooks* v. *Midas-International Corp.* (1977), 47 Ill. App. 3d 266, 361 N.E.2d 815.

The preamble to the reinsurance agreement entered into betweeen Amreco and Calvert recited:

> "An agreement of reinsurance between the American Mutual Reinsurance Company, Chicago, Illinois, (hereinafter called the 'Company') and Calvert Fire Insurance Company, Philadelphia, Pennsylvania (hereinafter called the 'Participant').
>
> Whereas the Company issues to insurance companies (hereinafter called individually as an 'Insurer') contracts and binders of reinsurance covering Property and Casualty lines of insurance and combinations thereof, and
>
> Whereas the Company desires to reinsure with the Participant a share of liability under each of such contracts and binders of reinsurance.
>
> Now therefore the Company agrees to cede and the Participant agrees to accept a share of liability under each such contract."

After stating the proportion of Calvert's liability for each contract, the agreement provided that liability was limited to the lesser of $300,000 or 7.5 per cent of Amreco's liability under the applicable insurance contract. The premium which Calvert was to receive for providing this reinsurance was 95.5% of Calvert's "proportionate share of the earned premiums paid by the Company (Amreco) on the contracts reinsured." Deducted from this premium were any premium adjustments paid on the contracts, and any premiums for reinsurance which might be obtained independently of the scheme of participation.

On appeal, Calvert readily acknowledges that it agreed to reinsure a portion of Amreco's contracts of reinsurance. However, it contends that the consideration received from Amreco was a security, since Calvert received a participatory share in

the reinsurance pool. Before reaching this question, however, we must determine whether the reinsurance pool constitutes "the business of insurance" and is thus exempt under the McCarran-Ferguson Act from federal securities laws.

Section 2(b) of the McCarran Act (15 U.S.C., §1012(b)) provides that "No Act of Congress shall be construed to invalidate, impair or supercede any law enacted by any State for the purpose of regulating the business of insurance * * * unless such act specifically relates to the business of insurance * * *." In *S.E.C.* v. *National Securities Inc.* (1969), 393 U.S. 453, 459-60, 89 S. Ct. 564, 568-69, 21 L. Ed. 2d 668, 676, the United States Supreme Court recited the history of the act[2] and defined its limits:

> "Given this history, the language of the statute takes on a different coloration. The statute did not purport to make the States supreme in regulating all the activities of insurance companies; its language refers not to the person or

2. "The McCarran-Ferguson Act was passed in reaction to this Court's decision in *United States* v. *South-Eastern Underwriters Assn.*, 322 U. S. 533 (1944). Prior to that decision, it had been assumed, in the language of the leading case, that '[i]ssuing a policy of insurance is not a transaction of commerce.' *Paul* v. *Virginia*, 8 Wall. 168, 183 (1869). Consequently, regulation of insurance transactions was thought to rest exclusively with the States. In *South-Eastern Underwriters*, this Court held that insurance transactions were subject to federal regulation under the Commerce Clause, and that the antitrust laws, in particular, were applicable to them. Congress reacted quickly. Even before the opinion was announced, the House had passed a bill exempting the insurance industry from the antitrust laws. 90 Cong. Rec. 6565 (1944). Objection in the Senate killed the bill, 90 Congr. Rec. 8054 (1944), but Congress clearly remained concerned about the inroads the Court's decision might make on the tradition of state regulation of insurance. The McCarran-Ferguson Act was the product of this concern. Its purpose was stated quite clearly in its first section; Congress declared that 'the continued regulation and taxation by the several States of the business of insurance is in the public interest.' 59 Stat. 33 (1945), 15 U.S.C. §1011. As this Court said shortly afterward, '[o]bviously Congress' purpose was broadly to give support to the existing and future state systems for regulating and taxing the business of insurance.' *Prudential Insurance Co.* v. *Benjamin*, 328 U.S. 408, 429 (1946)." 393 U.S. at 458.

companies who are subject to state regulation, but to laws 'regulating the business of insurance.' Insurance companies may do many things which are subject to paramount federal regulation; only when they are engaged in the 'business of insurance' does the statute apply. Certainly the fixing of rates is part of this business; that is what *South-Eastern Underwriters* was all about. The selling and advertising of policies, *FTC* v. *National Casualty Co.*, 357 U.S. 560 (1958), and the licensing of companies and their agents, cf. *Robertson* v. *California*, 328 U.S. 440 (1946), are also within the scope of the statute. Congress was concerned with the type of state regulation that centers around the contract of insurance, the transaction which *Paul* v. *Virginia* held was not 'commerce.' The relationship between the insurer and insured, the type of policy which could be issued, its reliability, interpretation, and enforcement—these were the core of the 'business of insurance.' Undoubtedly, other activities of insurance companies relate so closely to their status as reliable insurers that they too must be placed in the same class. But whatever the exact scope of the statutory term, it is clear where the focus was—it was on the relationship between the insurance company and the policyholder. Statutes aimed at protecting or regulating this relationship, directly or indirectly, are laws regulating the 'business of insurance.' "

We believe that the present reinsurance agreement meets the criteria set forth in *National Securities* since it is a closely related activity. Although it has been held that a reinsurance contract between two insurance companies does not involve the policyholder in that he lacks privity of contract with the reinsurer and has no right of action against it, (*Citizens Casualty Co. of N. Y.* v. *American Glass Co.* (7th Cir. 1948), 166 F. 2d 91), the ultimate purpose of the agreement is to provide reliable insurance to policyholders. Consequently, the agreement between Amreco and Calvert constitutes the "business of insurance" within the meaning of the McCarran-Ferguson Act.

The McCarran-Ferguson Act renders federal securities laws inapplicable when state legislation generally proscribes, permits,

or otherwise regulates the conduct in question and authorizes enforcement through a scheme of administrative supervision. *F.T.C.* v. *National Casualty Co.* (1958), 357 U.S. 560, 78 S. Ct. 1260, 2 L. Ed. 2d 1540; *Crawford* v. *American Title Ins. Co.* (5th Cir. 1975), 518 F. 2d 217; *Commander Leasing Co.* v. *Transamerica Title Ins. Co.* (10th Cir. 1973), 477 F.2d 77.

Not only does the Illinois Insurance Code (Ill. Rev. Stat. 1973, ch. 73, pars. 204.1 *et seq.*) provide a scheme of general state regulation of the business of insurance, but the Insurance Code also contains specific provisions pertaining to the regulation of reinsurance agreements between insurance companies under Article XI. (Ill. Rev. Stat. 1973, ch. 73, pars. 785 *et seq.*) These provisions govern the extent to which reinsurance may be accepted or ceded by a company, and sets forth the conditions under which credit may be taken for the reserves on such ceded risks.

Among other statutes and regulations, Illinois Department of Insurance Rule 9.23 requires a comprehensive report of all reinsurance activity, including information regarding premiums, and sets forth more elaborate requirements for obtaining reinsurance credit. Rule 11.01 further requires companies, upon request, to furnish copies of reinsurance agreements.

The instant case presents a transaction whereby Calvert agreed to insure a portion of each reinsurance contract entered into by Amreco with primary insurers. It is apparent that the parties entered into a reinsurance agreement, albeit one step further removed from the actual policyholder than conventional reinsurance. The agreement was therefore subject to the specific regulatory powers of Illinois concerning reinsurance. As such, characterizing as a security the premiums that would have been paid by Amreco provides no basis for a valid distinction. Amreco's payments, regardless of the form they may take, are subject to state regulation since ceded reinsurance premiums are under the control of the Director of the Department of Insurance. Thus, the McCarran-Ferguson Act precludes application of federal securities laws.

Furthermore, even without the McCarran-Ferguson Act, the Securities Act of 1933 and the Securities Exchange Act of 1934 would still be inapplicable since insurance contracts are not considered securities within the meaning of these acts. (*S.E.C.* v. *Variable Annuity Life Ins. Co.* (1959), 359 U.S. 65, 79 S. Ct. 618, 3 L. Ed.2d 640; *S.E.C.* v. *United Benefit Life Ins. Co.* (1967), 387 U.S. 202, 87 S. Ct. 1557, 18 L. Ed. 2d 673; *Tcherepnin* v. *Knight* (1967), 389 U.S. 332, 88 S. Ct. 548, 19 L. Ed. 2d 564.

Section 3(a)(8) of the Securities Act of 1933 provides:

> "(a) Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:
>
> '(8) Any insurance or endowment policy or annuity contract or optional contract, issued by a corporation subject to the supervision of the insurance commissioner * * * of any State or Territory or the United States or the District of Columbia;' 15 U.S.C. §77(c)(a)."

This provision has been considered to be "supererogation." (1 Loss, Securities Regulation 497 (2d ed. 1961).) Congress specifically stated that the subsection "makes clear what is already implied in the act, namely, that insurance policies are not to be regarded as securities subject to the provisions of the act." (H.R. Rep. No. 85, 73d Cong., 1st Sess., 15 (1933).) The definition of a security under both the 1933 and 1934 acts are virtually identical, and have been similarly construed. See *Tcherepnin* v. *Knight*[3] (1967), 389 U. S. 332, 88 S. Ct. 548, 19 L. Ed. 2d 564.

Calvert contends that the participants in the reinsurance pool supplied Amreco with investment capital in the form of con-

3. On occasion, a specific exemption under the 1933 Act has been held to be inapplicable to the 1934 Act absent express language. (*S.E.C.* v. *Ralston Purina Co.* (1953), 346 U.S. 119, 73 S. Ct. 981, 97 L. Ed. 1494.) Pertaining to insurance contracts, however, we believe that Congress did not intend that either act apply.

tractual commitments to indemnify Amreco. It is argued that the effect of these reinsurance commitments was to provide financing for Amreco's operations and to allow Amreco to enter into various reinsurance contracts which were to produce a profit for the pool.[4]

We perceive no difference between the traditional payment for insurance and the arrangement in the instant case, and therefore must reject Calvert's characterization of the reinsurance pool. Amreco agreed to pay a set premium for obtaining Calvert's commitment. That premium would not vary in any manner in that, unlike profits derived from an investment, Calvert's income from premiums was fixed by the contract. (Cf. *S.E.C.* v. *Variable Annuity Life Ins. Co. of America* (1959), 359 U.S. 65, 79 S.Ct. 618, 3 L. Ed. 2d 640; *S.E.C.* v. *United Benefit Life Ins. Co.* (1967), 387 U.S. 202, 87 S. Ct. 1557, 18 L. Ed. 2d 673.) Actual income to Calvert being dependent upon payments made to the primary policyholders for losses covered under their policies does not alter this fact. Precisely the same situation occurs in every contract of insurance. Viewing the transaction in this manner, it becomes apparent that Amreco's undertaking to pay premiums did not constitute a security. Although it has long been recognized that an insurance contract may contain elements of a security which may be separated from traditional insurance activities, (*S.E.C.* v. *United Benefit Life Ins. Co.* (1967), 387 U.S. 202, 87 S.Ct. 1557, 18 L. Ed. 2d 673) no such situation is involved here.

Insofar as the Illinois Securities Law (Ill. Rev. Stat. 1973, ch. 121½, par. 137.2-1 *et seq.*) and the Maryland Securities Act (32A Maryland Code Anno. §25(1)) are concerned, both employ definitions similar in approach to that of the federal acts.

4. Calvert vigorously urges us to hold that the arrangement involved is an investment contract which would be subject to the securities laws. "The test [for an investment contract] is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others." *S.E.C.* v. *W. J. Howey Co.* (1946), 328 U.S. 293, 301, 66 S.Ct. 1100, 1104, 90 L. Ed. 1244, 1251.

(See *Polikoff* v. *Levy* (1965), 55 Ill. App. 2d 229, 204 N.E.2d 807, cert. den. 382 U.S. 903.) The reasoning involved in exempting insurance policies from federal securities laws is equally applicable to holding that an exemption exists under state laws: "[A] savings accounts or insurance policy, like a corporate bond, subject the investor to some risk of capital loss in return for a relatively fixed return. These transactions are explicitly exempted from the registration requirements of the 1933 Act, 15 U.S.C. §77c, not because investors do not need protection, but because other agencies regulate the institutions involved." (*El Khadem* v. *Equity Securities Corp.* (9th Cir. 1974), 494 F.2d 1224, 1230, cert. den. 419 U.S. 900.) We believe the Illinois Department of Insurance has adequate means for regulating the insurance industry and therefore hold the Illinois Securities Act inapplicable. We assume that Maryland's policy pertaining to insurance contracts is similar. See *Colligan* v. *Cousar* (1963), 38 Ill. App.2d 392, 187 N.E.2d 292.

For the foregoing reasons, the judgment of the trial court striking and dismissing portions of defendant's answer and counterclaim is affirmed.

AFFIRMED.

DIERINGER, P.J., and JOHNSON, J., concur.

62120

AMERICAN MUTUAL REINSURANCE COMPANY, an Illinois corporation,
Plaintiff-Counterdefendant-Appellee,

v.

CALVERT FIRE INSURANCE COMPANY, a Pennsylvania corporation,
Defendant-Counterplaintiff-Appellant.

APPEAL FROM THE CIRCUIT COURT OF COOK COUNTY.

HONORABLE ARTHUR L. DUNNE, PRESIDING.

Mr. JUSTICE LINN delivered the Supplemental Opinion of the court upon the denial of the Petition for Rehearing:

In its petition for rehearing, Calvert urges us to reconsider our position in confining our examination to the pleadings in this case. It is contended that if the entire record were reviewed, a different conclusion would be reached. However, our holding would not be affected by such a review.

Were the whole record to be considered, Calvert would be allowed to raise two additional issues. Throughout these proceedings, Calvert has urged that the affidavit submitted by its president establishes that the arrangement between the parties was not regulated. The affidavit contains the statement: "The relationship between Amreco and the insurers participating in the Pool is not subject to any regulation by the State Insurance Department of Illinois." We do not believe that a legal conclusion by an affiant interested in the present litigation can be conclusive on this issue. Furthermore, we note that the affidavit was made a part of the record in this case on August 5, 1975, several weeks subsequent to the dismissal by the trial court on June 16, 1975. Therefore, its submission was not offered in a timely manner and could not have been considered even if the entire record were reviewed.

The second issue which Calvert contends should be considered is that the agreement must be judged as that which Amreco represented it to be. It is asserted that Amreco used the terms "profits" and "investment," in its dealings with Calvert, and therefore the participatory interest should be held to be a security. We do not see the relevance of Amreco's use of the word "profits," since many undertakings, other than investments, are entered into with an expectation that the venture will prove profitable. Also, an examination of the record reveals that only after Calvert had entered into the pool did Amreco colloquially describe the arrangement as an investment. Although it is not inappropriate that an offering be judged as being what it is represented to be, (*S.E.C.* v. *C.M. Joiner Leasing Corp.* (1943), 320 U.S. 344, 64 S. Ct. 120, 88 L. Ed. 88), such a standard is inapplicable in a case such as the present one. Calvert was not induced to enter into the pool due to any representation by Amreco that participation constituted an investment.

Since these points raised by Calvert do not affect the outcome of this case, the judgment of the trial court stands as stated in our opinion and the Petition for Rehearing is denied.

DIERINGER, P. J., and JOHNSON, J., concur.

APPENDIX H

No. 62120

IN THE APPELLATE COURT OF ILLINOIS

FIRST JUDICIAL DISTRICT

AMERICAN MUTUAL REINSURANCE COMPANY, an Illinois corporation, *Plaintiff-Counterdefendant-Appellee,*	APPEAL FROM THE CIRCUIT COURT OF COOK COUNTY.
v.	—
CALVERT FIRE INSURANCE COMPANY, a Pennsylvania corporation, *Defendant-Counterplaintiff-Appellant.*	Hon. Arthur L. Dunne, Presiding.

ORDER

This cause coming on to be heard on the motion of CALVERT FIRE INSURANCE COMPANY, appellant, for a Certificate of Importance under Supreme Court Rule 316, and it appearing that this court inadvertently overlooked denying the petition for a Certificate of Importance at the time the Petition For Rehearing was denied:

IT IS THEREFORE ORDERED that the appellant's petition for a Certificate of Importance under Supreme Court Rule 316 is hereby denied.

ENTER:

/s/ HENRY W. DIERINGER
Presiding Justice

/s/ DAVID LINN
Justice

/s/ GLENN T. JOHNSON
Justice

DATED: October 12, 1977

APPENDIX I

State of Illinois
Office of
CLERK OF THE SUPREME COURT
Springfield
62706

Clell L. Woods, Clerk

Telephone
Area Code 217
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January 26, 1978

Mr. Michael L. Weissman
Attorney at Law
Aaron, Aaron, Schimberg & Hess
33rd Floor East
One First National Plaza
Chicago IL 60603

No. 50085—American Mutual Reinsurance Company, an Illinois Corporation, respondent, vs. Calvert Fire Insurance Company, a Pennsylvania Corporation, petitioner. Leave to appeal, Appellate Court, First District.

The Supreme Court today denied the petition for leave to appeal in the above entitled cause.

Very truly yours,

/s/ CLELL L. WOODS
Clerk of the Supreme Court

IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-1361

CALVERT FIRE INSURANCE COMPANY,
A PENNSYLVANIA CORPORATION,
Petitioner,

vs.

AMERICAN MUTUAL INSURANCE COMPANY,
AN ILLINOIS CORPORATION,
Respondent.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE ILLINOIS APPELLATE COURT.

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BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE ILLINOIS APPELLATE COURT.

QUESTIONS PRESENTED.

I. Does the judgment of the Illinois Appellate Court on an interlocutory appeal from an interlocutory order deciding only one issue in the case, on the pleadings, which issue may become moot, present a judgment appropriate for the issuance of the writ of certiorari to the Illinois Appellate Court?

II. Does the judgment of the Illinois Appellate Court, which presents no important question of federal law and creates no conflict of decision and which, if reversed, would be subject to reinstatement after presentation of evidence and consideration of a defense under federal law not yet at

issue, present a judgment appropriate for the issuance of a writ of certiorari to the Illinois Appellate Court?

STATEMENT OF THE CASE.

Petitioner states that its statement of the case is taken from the opinion of the Illinois Appellate Court but chooses to characterize the facts in a manner not done by the Illinois Appellate Court. Respondent respectfully directs the Court's attention to the Statement of Facts set forth in the opinion of the Appellate Court.[1]

The litigation was commenced in July of 1974 when American Mutual Reinsurance Company ("American Mutual") filed a simple contract action against Calvert Fire Insurance Company ("Calvert") in the Circuit Court of Cook County, Illinois. American Mutual in its complaint alleged that Calvert breached its reinsurance contract with American Mutual whereby Calvert agreed to provide reinsurance for American Mutual. Calvert was the only one of the one hundred reinsurers having similar, separate, contracts with American Mutual which attempted to avoid its liability under its reinsurance contract.

Not until some six months after the filing of the action did Calvert file an answer and counterclaim alleging as defenses and in support of its counterclaim that American Mutual had made misrepresentations with reference to the contract, and alleging violation of the federal, Illinois and Maryland securities laws.

The Circuit Court of Cook County sustained American Mutual's motion to dismiss only those portions of Calvert's answer and counterclaim based upon the federal and Illinois and Maryland securities laws. On interlocutory appeal from that order, the Illinois Appellate Court affirmed the order of the trial court. The remaining issues in the case are pending for trial in the Circuit Court of Cook County.

1. Appendix G to Petition.

REASONS FOR DENYING THE WRIT OF CERTIORARI.

Summary of Argument.

The petition should be denied because the judgment of the Illinois Appellate Court is not final for purposes of certiorari and may be rendered moot by further proceedings. Even if reversed, the judgment could be reinstated after presentation of legal defenses not yet of issue and evidence.

The issues presented on this petition are not related in any way to the issues presented to this Court in the case of *Will* v. *Calvert Fire Insurance Co.* (U. S. No. 693, 1977 Term). That case presents the questions of whether the District Courts of the United States have been deprived of all discretion to stay proceedings before them in any case involving a claim of a right arising under a federal law and whether a mandamus should issue from a Court of Appeals to a United States District Court to require an immediate adjudication of any federal claim when the identical legal issues are pending in the state courts between the same parties.

There is no important question of federal law presented by the petition nor is there any conflict of decision arising from the decision of the Illinois Appellate Court. The so-called "security" issue (the quotation marks are Calvert's) raised by petitioner is unique. It has never before been presented to a court and may well never be presented again because of the unusual nature of the facts in this case.

Finally, the decision of the Illinois Appellate Court is correct and follows the laws interpreted by this Court. Two different courts have held, and a third announced that it would hold, that the insurance transaction in question did not constitute the sale of a security.

I.

The Decision of the Illinois Appellate Court Is Not Final for Purposes of Certiorari and the Issue Decided May Become Moot.

The petitioner prays that a writ of certiorari should issue to review a judgment of the Illinois Appellate Court which affirmed an interlocutory order of the Circuit Court of Cook County striking and dismissing portions of petitioner's answer and counterclaim insofar as they alleged defenses and counterclaims based upon the federal and state securities laws.

The judgment of the Illinois Appellate Court is not a final judgment under Title 28 U. S. C. §1257 as interpreted by this Court.[2] Nor does the judgment of the Illinois Appellate Court come within any of the exceptions to the rule of finality as enunciated by this Court,[3] and petitioner does not claim that it does.

The petitioner appears to concede that the judgment is not final (petition, p. 9) and states that it would be "unusual" for this Court to grant the writ of certiorari to review an interlocutory judgment of this type.

The case giving rise to the issue presented by Calvert's petition for certiorari is still pending in the Circuit Court of Cook County and no trial has been had and no final judgment has been entered. The remaining issues in the case, including Calvert's defense and counterclaim based upon allegations of fraud, are yet to be adjudicated.

If Calvert should sustain its defense or counterclaim based upon fraud, the order striking its "security" claims would become moot.

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2. *Republic Natural Gas Co.* v. *Oklahoma*, 334 U. S. 62 (1948); *Radio Station WOW, Inc.* v. *Johnson*, 326 U. S. 120 (1945); *Gospel Army, Inc.* v. *Los Angeles*, 331 U. S. 543 (1947).

3. *Cox Broadcasting Corp.* v. *Cohn*, 420 U. S. 469 (1975).

If Calvert should not prevail on trial, it would have the right to seek review after final judgment in the Illinois courts, and ultimately, to petition this Court for a writ of certiorari to review the very issue presented by the present petition, if it would then be a viable issue.

In an attempt to bestow an aura of finality upon the order striking portions of its pleadings which was affirmed by the Illinois Appellate Court, Calvert contends that if this Court should determine that the sale of reinsurance by Calvert for a premium constituted a purchase of a "security" by Calvert, that Calvert would be entitled to "automatic rescission" of its contract under the Securities Act of 1933.

Petitioner ignores the fact that if this Court should so hold, at most, a fact question under the securities law would be presented to the Circuit Court of Cook County, determinable only after the presentation of evidence.

Petitioner also ignores the fact that if this Court should determine that the transaction constituted the purchase of a "security" that on remand to the Circuit Court of Cook County, American Mutual would then be required to plead to the "security" issue and would plead as a defense that the transaction was exempted from registration available under § 4(2) of the 1933 Act. (15 U. S. C. § 77d(2)) Because no court has yet held that the transaction constitutes the sale of a "security" the assertion of that defense would have been premature in prior proceedings.

There are, therefore, an issue of federal law and issues of fact, potentially determinative of the merits of the "security" issue, which have not yet been adjudicated.

II.

The Issues Presented by the Petition for Writ of Certiorari Are Entirely Separate from the Issues Before This Court in the Case of Will v. Calvert Fire Insurance Co.

The case of *Will* v. *Calvert Fire Insurance Co.* (U. S. No. 693, 1977 Term), in which this Court granted a writ of certiorari to the Court of Appeals for the Seventh Circuit, concerns questions totally unrelated to the issues presented by Calvert's petition for a writ of certiorari. The issues presented in the *Will* case are (1) whether the District Courts have been deprived by this Court's decision in *Colorado River Water Conservation District* v. *United States*, 424 U. S. 800 (1976), of all discretion to stay proceedings pending before them in the interest of judicial economy and to avoid duplicative litigation, (2) whether the United States District Courts have a clear legal duty enforceable by mandamus "immediately" to try cases before them despite the fact that prior commenced litigation between the same parties raising the same legal and factual issues, is proceeding in a state court in a manner that may well render the entire federal case moot, and (3) whether this Court's opinion in *Colorado River* entitles a litigant effectively to compel a United States District Judge by writ of mandamus to engage in a race with the state court to decide identical legal issues pending in both courts between the same parties when the judge reasonably believes such race to be unnecessary and wasteful.

The issues raised in the *Will* case relate solely to the discretion of a United States District Judge to defer ruling on a federal question when that same question is being litigated in another court. There is no substantive question of federal securities law presented to this Court in the *Will* case, but only questions of procedure.

Calvert's petition does not in any way intimate there is a relationship between the issues presented by its position and the issues in the *Will* case.

The granting of the petition for writ of certiorari in this case would in no way eliminate or simplify the issues presented in the *Will* case.

III.

There Is No Important Question of Federal Law Presented by the Petition or Any Conflict of Decision Arising from the Decision of the Illinois Appellate Court.

Petitioner does not appear to even attempt to advise this Court that the "securities" issue presented by its petition presents an important question of federal law nor does Calvert point out any conflict of decision arising from the decision of the Illinois Appellate Court.

The fact situation upon which Calvert predicates its claim of the existence of a "securities" issue, is both narrow and unique. A reinsurance pool is an arrangement whereby various reinsurers, such as Calvert, particpate in reinsuring risks undertaken by various primary insurance companies. It is an arrangement which can be entered into only by insurers licensed by the states to participate in reinsurance. It amounts to insurance of insurance companies by other insurance companies. It is not an investment scheme as urged by Calvert, but is an arrangement limited only to certain insurance carriers. Calvert presents no issue as to the sale of securities to the investing public.

It is noteworthy that the federal securities laws are rapidly approaching their 50th anniversary of enactment and no other litigant has ever contended that a reinsurance pool arrangement or the sale of reinsurance by it constitutes the purchase of a security. The issue may never be raised again.

The narrow "securities" issue presented by Calvert is so limited that none of the ninety-nine other insurance carriers which entered into reinsurance contracts with American Mutual attempted to rescind its contract nor did any claim that the sale by them of reinsurance constituted the purchase by them of a "security".

The decision of the Illinois Appellate Court does not raise any important question of federal law, and does not in any way modify the established practice within the reinsurance industry. It merely reaffirms the understanding of the insurance industry that the sale of reinsurance is the sale of insurance and not the purchase of a "security".

And, of course, there is no conflict of decision created by the decision of the Illinois Appellate Court for the same reason. No court has ever been asked before, and no court may ever be asked in the future, to hold that the sale of reinsurance by a reinsurer, such as Calvert, constitutes the purchase of a "security" by the reinsurer.

IV.

The Decision of the Illinois Appellate Court Is Correct and in Accordance with the Decisions of This Court.

The Illinois Appellate Court in arriving at its decision carefully followed the guidelines laid down by this Court both in determining whether the sale by Calvert of reinsurance constituted a purchase of a "security" and whether the McCarran-Ferguson Act precluded the application of the federal securities laws to this fact situation.

Calvert takes a numerical approach to this case by implying that because this Court has construed the term "security" to include various investment plans in five of six cases, that it may be likely that this Court will construe the term "security" to encompass the reinsurance contract in question.

The fact that this Court has found the sale of real property interests, sales of variable annuities, and savings accounts to be within the definition of a security provides no support for Calvert's argument that the reinsurance contract in question constituted the sale of a security.

On the contrary, the teaching of this Court in *SEC* v. *Variable Annuity Life Insurance Co. of America*[4] and *SEC* v.

4. 359 U. S. 65 (1959).

United Benefit Life Insurance Co.[5] compels the conclusion that the reinsurance contract in question cannot be construed to be a security. The Illinois Appellate Court carefully followed this Court's guidelines in so holding.

As the legislative history of the Securities Act of 1933 and Professor Loss[6] make clear, the intent of the 1933 Act is that insurance policies and like contracts are not regarded as investment securities subject to the provisions of the Act.

Nor is it surprising that in two cases involving the sale by insurance companies of variable annuity contracts, this Court held such sales to be sales of an investment. The distinctions between the *Variable Annuity* and *United Benefit* cases and the Calvert transaction are numerous.

Neither case involved a contract of reinsurance, but both involved a variable annuity which neither Calvert nor American Mutual is authorized to sell. In the two variable annuity cases, the insurance company invested the premium with an agreement to return the proceeds. There was no investment by American Mutual for Calvert's benefit and no return of proceeds. The reason for this Court's holding in *Variable Annuity* and *United Benefit* that variable annuity contracts were not insurance policies, was that there was no underwriting of risks by the companies but merely an agreement to pay back the proceeds of investment.[7] In the instant case, underwriting risks were undertaken by both American Mutual and Calvert and results were dependent upon the acts of nature and the insurance experience of the primary insurance carriers. Further, Calvert did not buy a policy as did the purchasers of the variable annuity policies in *Variable Annuity* and *United Benefit*. It sold insurance to American Mutual.

5. 387 U. S. 202 (1967).

6. H. R. Rep. No. 85, 73rd Cong., 1st Sess. 15 (1933); 1 Loss, Securities Regulations 497 (2d Ed. 1961).

7. 359 U. S. 65, 71 (1959); 387 U. S. 202, 211 (1967).

Finally, in *Variable Annuity* and *United Benefit*, the policies were sold by insurance companies to the unsophisticated public in return for money. American Mutual did not sell a security to the public but it entered into a contract of reinsurance with Calvert whereby Calvert agreed to reinsure American Mutual.

Petitioner also contends that the Illinois Appellate Court did not follow the teaching of this Court in *SEC* v. *W. J. Howey Co.*, 328 U. S. 293 (1946) wherein this Court defined the test for an investment contract.

A reading of the opinion of the Illinois Appellate Court[8] indicates to the contrary. The Illinois Appellate Court quoted the test set down by this Court in *Howey* and pointed out that the reinsurance contract sold by Calvert did not meet the *Howey* test because it was a conventional insurance agreement whereby Calvert agreed for a fixed premium to reinsure certain risks. The Illinois Appellate Court noted that the fact that Calvert's ultimate income might be dependent upon losses under the policy does not alter the result because precisely the same situation occurs in every contract of insurance. As this Court has pointed out, underwriting of risks is "the one earmark of insurance as it has commonly been conceived of in popular understanding and usage."[9]

And, it is precisely because the contract in question partook of the very essence of insurance, *i.e.*, the underwriting of risks, that the Illinois Appellate Court quite properly held that the agreement constituted the "business of insurance" and that the McCarran-Ferguson Act by its express terms precluded the application of the federal securities laws to the transaction. In so doing, the Illinois Appellate Court followed the directions given by this Court in determining whether the transaction constituted the "business of insurance."[10]

8. Appendix G of Petition.

9. *SEC* v. *Variable Annuity Life Ins. Co.*, 359 U. S. 65, 73 (1959).

10. *SEC* v. *National Securities, Inc.*, 393 U. S. 453, 459 (1969); *SEC* v *Variable Annuity Life Ins. Co.*, 359 U. S. 65, 68 (1959).

The detailed regulatory scheme of the Illinois Department of Insurance regulating insurance carriers and reinsurance activity, as set forth in the opinion of the Illinois Appellate Court, would be impaired, if not invalidated, and superseded if the federal securities acts were construed as urged by Calvert. Such a construction would be contrary to the express terms of the McCarran-Ferguson Act as construed by this Court.[11]

Finally, it is noteworthy that three different courts have already considered the "security" issue. The Circuit Court of Cook County held that there was no "security" as did the Illinois Appellate Court in a full, carefully reasoned opinion. Judge Will, who was of the opinion that it was premature to consider this issue, has stated that if called upon to decide the issue on the merits, he, too, would decide that there was no sale of a "security" to Calvert.[12]

The decision of the Illinois Appellate Court is not only correct but is in complete accord with the controlling decisions of this Court.

CONCLUSION.

It is therefore respectfully submitted, for the reasons set forth above, that Petition for Writ of Certiorari be denied.

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11. *FTC* v. *National Casualty Co.*, 357 U. S. 560 (1958).

12. Transcript of Proceedings before the Hon. Hubert L. Will on June 18, 1975 at 3, *Calvert Fire Insurance Co.* v. *American Mutual Reinsurance Co.*, No. 75 C 103 (N. D. Ill., 1975).